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CIS

REVIEW OF 1981 BLOCK GRANTS

HEARING

BEFORE THE

SUBCOMMITTEE ON INTERGOVERNMENTAL RELATIONS

OF THE

COMMITTEE ON GOVERNMENTAL AFFAIRS UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

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REVIEW OF 1981 BLOCK GRANTS

THURSDAY, NOVEMBER 5, 1981

U.S. SENATE,
SUBCOMMITTEE ON INTERGOVERNMENTAL RELATIONS,
COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, D.C.

The subcommittee met at 10:05 a.m. in room 318, Russell Senate Office Building, Hon. David Durenberger (chairman of the subcommittee) presiding.

Present: Senators Durenberger, Danforth, Mattingly, and Nunn.

Also present: Senators Stafford and Domenici.

OPENING STATEMENT OF SENATOR DURENBERGER

Senator DURENBERGER. The hearing will come to order.

This morning the Subcommittee on Intergovernmental Relations returns to the subject of block grants which we have explored in great depth on many occasions in the past year. This particular hearing is being held at the request of the National Governors' Association which sought an opportunity to offer a clear and concise summary of its views on the new federalism as we begin a new round of budget considerations.

The subcommittee is pleased with the opportunity to sponsor this hearing. We are honored by the witnesses who will be with us this morning. We have only three witnesses. They are the current chairman of the National Governors' Association, Gov. Richard Snelling of Vermont; the past chairman of the NGA, Gov. George Busbee of Georgia; and the incoming chairman of the association, Gov. Scott Matheson of Utah. It is my understanding that this is the first time that such a group of Governors has appeared before the Congress. Their presence speaks to the importance of the issues we will be considering this morning.

The hearing has been described as a review of the block grants that were created in the reconciliation process last spring and summer. Block grants will certainly be an important focus for our discussion. In a broader sense, block grants are only a surface indication of the very sweeping changes that are being made in the intergovernmental system.

Our purpose this morning is to consider that system as a whole and its future in light of the budget realities facing the Congress. From the perspective of the National Government, the intergovernmental system is an $85 billion pipeline that provides assistance to State and local governments through some 500 separate grant programs. That $85

billion is a large portion of the discretionary spending of the Federal Government. Most of the rest of the Federal budget is tied up in defense, entitlements and interest payments on the national debt.

It is obvious to everyone, including the Governors who will speak in a few minutes, that the budget problems of the Federal Government will have a significant impact on the programs of State and local governments. We are faced with the difficult task of sorting through the many commitments which we have made over the last 20 years in the name of a better society for today and tomorrow. The one commitment we must keep constantly before us is the resolve of this Nation to do only as much of government as we need and as close as possible to the people who need it. As we work to remake the budget of the National Government, we will be returning significant responsibilities to the States, the cities, the counties and the towns of America. We should all welcome the return of government to the courthouses, city halls and State capitals across the country.

We must also understand the capacity and the machinery of State and local governments. In the process of redefining federalism, we must take care that we do not discredit that very form of government—the Federal form of government. It is a government that we value. By failing to understand the realities facing our partners in the intergovernmental system, we face failure.

Our purpose this morning is to further that understanding and bring the opportunity of a New Federalism closer by joining in a dialog with the leadership of the National Governors' Association.

We will make a serious attempt to conduct this hearing as a dialog. No subject in the intergovernmental system will be out of bounds. I will encourage every Senator who attends to join in the dialog at whatever point seems appropriate.

Do any of the other Senators wish to make an opening statement?

Senator Stafford, do you want to make some comments about these three people whom you know so well?

OPENING STATEMENT OF SENATOR STAFFORD

Senator STAFFORD. Mr. Chairman, thank you very much.

I came here really to say a word or two about Governor Snelling because he is the Governor of the State I have the honor of representing here in the U.S. Senate. I also have known Governor Busbee and Governor Matheson for a number of years through involvement of the Committee on Environment and Public Works and various activities in their States, in fact all of the States of the Nation.

But I appreciate this honor particularly to have a chance to say that I have known Governor Snelling throughout my own career in statewide politics in Vermont. He has been an unusually successful businessman in our State. He had been a very able member of the Vermont Legislature before he became Governor. He was a majority leader in Vermont's House. In the view of most Vermonters, he is one of the most able and successful Governors that we have ever been graced with.

So I came here this morning to indicate my own admiration for Governor Snelling, his accomplishments, particularly as chairman of the National Governors' Association, an honor that no other Vermont

Governor has been able to achieve in the past. So I am sure his words will be taken with the weight they are entitled to in front of this subcommittee, as will the other Governors, one of whom has preceded him and one of whom will follow.

Thank you very much, Mr. Chairman.

Senator DURENBERGER. Thank you.

Senator Nunn?

OPENING STATEMENT OF SENATOR NUNN

Senator NUNN. Mr. Chairman, I thank you for calling these hearings. I have had many discussions with Governor Busbee about some of the opportunities and challenges of the new economic program and the new move toward a different kind of governmental relationship between Federal and State governments. I know he has been an outstanding leader in the National Governors' Association for a long time.

I have heard a lot about Governor Snelling. I have met with Governor Matheson and had some detailed conversations with him about some of the dilemmas that we face.

I have a statement I would like to put in the record, but I would like to just say that I think we are in somewhat the same situation, at least the Governors are, that the United States was in back around the early 1900's when we were about to get into a war with Germany and the German submarine fleet was sinking ships all over the Atlantic. Will Rogers was asked at that time how he would deal with the growing German submarine threat. He said, "It is very simple. We just drain the Atlantic Ocean and that will end the threat." He was then asked, "Mr. Rogers, how do we drain the Atlantic Ocean?" He replied, "I am a generalist and that is a detail." [Laughter.]

I believe that is somewhat analogous to the situation the Governors find themselves in now, and not just the Governors but the city and county governments. I think we have laid down a general policy here in Washington. We have left it up to them to handle the details. Yet, the details are becoming almost unmanageable at the State level.

So I am interested in hearing from Governors Busbee, Snelling, and Matheson this morning. I will simply put the remainder of my statement in the record.

Senator DURENBERGER. They will be praying we don't pull the plug on them. [Laughter.]

Thank you very much, Senator. Your statement will be made a part of the record.

[Senator Nunn's prepared statement follows:]

PREPARED STATEMENT OF SENATOR NUNN

Thank you, Mr. Chairman. I am pleased to join you and other members of the Intergovernmental Relations Subcommittee in welcoming Governors Snelling and Matheson and my own Governor, Governor George Busbee.

I am also pleased that we have been joined by our other colleagues because I believe that the issues which we will be examining this morning raise fundamental questions regarding the future role of both state and federal government in our nation's system of federalism.

With the passage earlier this year of the Omnibus Reconciliation Act, Congress inaugurated a new era in American federalism by beginning the implementation of block grant programs to the states. The Omnibus Reconciliation Act

consolidated 57 former categorical programs with total authorizations of $7.6 billion for fiscal year 1982 into 9 functional areas of block grants.

The block grant concept marks a significant alteration of past funding arrangements between federal, state and local governments. This consolidation of federal assistance designates the state government as primary recipient and decisionmaker. Most importantly, we must realize—here in Washington—that by creating block grants we are calling on our states to administer more programs with less money.

Our state governments are now involved in seeking solutions to the challenges and changes proposed by this shift from categorical to block grants. The experience of these Governors in the implementation of this new strategy for the delivery of services to our shared constituency, and their observation on the effect of a reduced federal budget on the budgets of our state and local governments, must serve as an important guide-post in the future development of our economic policy.

We must realize that our state and local governments are currently being battered by reduced federal support, a federally initiated reduction in their own tax revenues—in addition to unprecedented high interest rates which currently plague our whole economy.

The citizens of this nation will be ill-served if the economic programs which we are in the process of implementing at the federal level succeed in balancing the federal government but bankrupting our state and local governments.

Mr. Chairman, I am pleased to be a part of the beginning of this essential dialogue between Congress and these Governors during this time of uncertainty, challenge and change in our federal-state relations.

Senator DURENBERGER. Senator Mattingly?

OPENING STATEMENT OF SENATOR MATTINGLY

Senator MATTINGLY. I would like to join my colleagues in welcoming you all here, Governors Snelling and Matheson and especially Governor Busbee. I think in the short time that I have been in the U.S. Senate, through my relationship with especially Governor Busbee, that he has helped us all greatly through his work this year with us in the Senate in trying to make this New Federalism, which he is such a great proponent of, and for which he has worked very closely with the President.

But in the beginning of the New Federalism came the block grants. I guess we could go into many of the inequities in any new program. But I feel that what will happen now is that with the help of these Governors—and I am especially proud of my own Governor—we will now get to the point where we will refine what has been started this year so there can be established a firm program that not only Governors can live with but the Federal Government can live with and which will benefit all of the people of our country.

I would like to point out, and not at the expense of saying too little about my other two friends here, but Governor Busbee has been an outstanding person this year and was a tremendous focal point in many of the actions that we took on the Senate floor. I would just like to personally commend him for that, and mention the continued respect that I have for him and you other two. Once again I repeat that now is the time to refine what we have done.

Senator DURENBERGER. Bob, let's go back to you before we go to Pete.

Senator STAFFORD. Thank you very much again, Mr. Chairman. I simply want to say to your guests in the audience and to the three Governors who are here that I am supposed to be presiding over the Committee on Environment and Public Works this morning. We are

struggling with the clean air legislation, which is I think of interest to all of the Governors here.

Having said that, with apologies to Governors Snelling, Matheson, and Busbee, I hope you understand why I should go to that meeting. I am taking your speeches with me, incidentally.

Thank you very much, Mr. Chairman.

Senator DURENBERGER. Thank you, Bob.

We are pleased to be joined today by the distinguished Senator from New Mexico who is the chairman of the Budget Committee, Pete Domenici.

Pete, do you have any comments you would like to make?

I am sure you do.

OPENING STATEMENT OF SENATOR DOMENICI

Senator DOMENICI. Mr. Chairman, thank you very much. I too want to welcome the Governors here and compliment you for this set of hearings.

Mr. Chairman, I do have a statement. I would say to you and your subcommittee and staff that I have affixed to this statement a recap of the block grants in the reconciliation bill. I think it is a total compilation and is pretty accurate. I think it will serve as a useful tool as you move through your deliberations. I would ask that that appendix be made a part of the record.

Senator DURENBERGER. It will be made part of the record. I thank you for it.

Senator DOMENICI. Mr. Chairman, I think it is essential that Federal, State and local governments, in cooperation with outside experts and public interest groups, undertake a new effort to revitalize the Federal system. The experiences of the last decade have shown us clearly that complex, highly regulated and duplicative Federal programs solve few of the problems that they were designed to attack. The so-called taxpayers' revolt and, indeed, the 1980 election results, reflected, in my opinion, the judgment of a majority of voters that government at all levels was not delivering results that were commensurate with the growing investment of tax dollars—and I might add, borrowed dollars—for the government programs.

After completing a 3-year study of the Federal system, the Advisory Commission on Intergovernmental Relations, ACIR, has found today's intergovernmental system a "bewildered and bewildering maze of complex, overlapping, and, often, conflicting relationships among the three levels of governments." More simply put, ACIR says that today's intergovernmental system is "overloaded" and needs to be "decongested."

A look at today's Federal grants-in-aid system compared with the system which existed in the sixties, 20 years ago, confirms this overload. In 1960, Federal programs providing funds to State and local governments numbered approximately 130 at a cost of about $7 billion. Today, Mr. Chairman, there are nearly 500 grant programs in place, with a price tag of about $90 billion.

Few strings were attached to the receipt of Federal funds two decades ago. Today, it is estimated that there are at least 1,350 separate Federal mandates which apply to State and local governments.

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There has been a proliferation of limited-purpose organizations, special districts, and planning bodies in this period, in many cases spawned by the Federal Government. The explosion of these types of "para-governments" has fragmented accountability and made the coordination and policy direction tasks of State and local general-purpose governments extremely difficult.

Now, Mr. Chairman, I am going to move from my prepared remarks and ask that where I have skipped them in my opening remarks that they be made a part of the record.

I want to move to page five.

The Omnibus Reconciliation Act provided some much-needed consolidation and simplification and increased State and local flexibility on the use of Federal grant funds in a number of cases. The eight blocks that were created are, as I indicated, detailed in the appendix.

Now, Mr. Chairman, I want to make one concrete suggestion and then I will yield and I hope to join you and hear our Governors.

I would like to propose to the subcommittee, Mr. Chairman, and the Governors, that you consider a further important step in program consolidation and increased flexibility for the States. I would call the idea that I want to describe very briefly as "megablock."

The "megablock," as I visualize it, would be a State-designed consolidation of Federal funding and programs. The Federal Government could invite a limited number of States, perhaps 8 or 10, to propose a package of programs to be consolidated on a trial basis. One group of States might propose, for example, to pool Federal and State funding of AFDC, food stamps, medicaid, social services, and perhaps other programs, into a single, integrated State plan for meeting financial, health care, and social service needs for low-income people. Other States might propose "megablocks" in the fields of education, housing and community development, transportation, et cetera.

They would even be permitted in these proposed State "megablocks" to sort out roles and responsibilities of the different levels of government. The plans would have to be multiyear in nature.

The key point is that we should test out a variety of comprehensive consolidated program options without undertaking them on a nationwide basis all at once. I am convinced that had the Nixon administration proposed major statewide demonstrations of some of its New Federalism concepts in the early seventies, we would be much further down the road to grant reform than we are today. But as you know, that administration sought the immediate beginning of several major block grants all at once. It didn't fly then and I submit it won't fly now.

The States receiving "megablocks" would be free to spell out the details of how they would operate them, subject only to some minimal criteria. For instance, it would be appropriate, and probably a prerequisite for starting such experiments, that States be required to demonstrate that they would have safeguards in place to assure equitable distribution of benefits under the consolidated program.

It would also be essential to provide standards and evaluation processes and procedures to assess the success of the State experience. The standards would need to be kept simple. They should just answer 4 or 5 years down the road the simple question: "Were the Federal resources used for their intended purposes at least as effectively and efficiently as they would have been had we kept the categorical ap-

proach?" If the answer is clearly "yes," then the experiment would be successful.

Mr. Chairman, I would submit that there is also an opportunity in this approach for the National Government, once it has a series of proposals, to select the recipients based upon how well the States have accommodated local versus State problems—cities and States. Make that an up-front criteria—how well they have solved the intergovernmental problems of funding and financing of the lower units of government. I would remind the subcommittee and the Governors that while we listen to them, you listen to a mayor from New York. He is very worried about the fact, Senator Nunn, that you can come up with a block, but who is going to make sure that the State takes care of the cities? There is almost as much friction going on there as there is between the National Government and the States.

We could make one of the criteria for selecting a State be that it design its plan so that it showed how well State and local leaders had begun to solve those kinds of problems.

I have a few more details in my statement, Mr. Chairman. I apologize for going on so long. I would ask that it be made a part of the record. I thank you for inviting me.

Senator DURENBERGER. We deeply appreciate your participation, Senator. It is both an interesting suggestion and, as a lot of us know, an indication of your very firm commitment to making this Federal system work by making the resources available and making some sense of the expenditure decisions.

Your full statement will be made a part of the record.

[Senator Domenici's prepared statement and "Summaries of Block Grant Provisions of 1981 Omnibus Reconciliation Act" follow:]

PREPARED STATEMENT OF SENATOR PETE V. DOMENICI

Mr. Chairman, it is indeed an honor to be here today to participate in the dialogue between this subcommittee and governors who are providing strong and creative leadership in the area of intergovernmental relations.

It is essential in my view that Federal, State and local governments, in cooperation with outside experts and public interest groups, undertake new efforts to revitalize the Federal system. The experiences of the last decade have shown clearly that complex, highly regulated and duplicative Federal programs solve few of the problems they were designed to attack. The so-called "taxpayers' revolt," and indeed the 1980 election results, reflected the judgment of a majority of voters that government at all levels was not delivering results commensurate with the growing investment of tax dollars—and borrowed dollars!—in government programs.

NEED FOR REFORM

After completing a three-year study of the Federal system, the Advisory Commission on Intergovernmental Relations (ACIR) has found today's intergovernmental system a "bewildered and bewildering maze of complex, overlapping, and, often, conflicting relationships among the three levels of government." More simply put, ACIR says today's intergovernmental system is "overloaded" and needs to be "de-congested."

A look at today's Federal grants-in-aid system compared with the system which existed in 1960, twenty years ago, confirms this "overload." In 1960, Federal programs providing funds to State and local governments numbered approximately 130 and cost a little over $7 billion. Today, nearly 500 grant programs are in place with a price tag of about $90 billion.

Few strings were attached to the receipt of Federal dollars two decades ago. Today, it is estimated that at least 1350 separate Federal mandates apply to State and local governments.

There has also been a proliferation of limited-purpose organizations, special districts and planning bodies in this period, in many cases spawned by Federal

requirements. The explosion of these types of "para-governments" has fragmented accountability and made the coordination and policy direction tasks of State and local general-purpose governments extremely difficult.

ACIR reports that the addition of more programs, more dollars, and more strings has made the Federal Government's influence at the State and local level "more pervasive, more intrusive, more unmanageable, more ineffective, more costly, and, above all, more unaccountable."

During my service as mayor of Albuquerque, New Mexico, I was involved in the early development of the forerunner of one of today's consolidated grant programs—the Comprehensive Employment and Training (CETA) program. Specifically, in Albuquerque, we consolidated many of the federal categorial manpower programs into a unified, integrated pool of funds which gave us the flexibility to adapt a set of programs to our local needs. This experiment helped form the pattern from which CETA emerged.

In the Senate, I have pushed for program consolidation and for increased flexibility at State and local levels on the use of Federal grant funds. Former Senator Bellmon and I authorized two optional grant consolidation bills in the areas of education and food and nutrition. Unfortunately—while the Senate passed a pilot-test version of the Child Nutrition bill—we did not have much success with these bills in Congress, or overwhelming support for them from State and local government groups.

DEVELOPMENTS IN THE 1970'S

I was encouraged during the Nixon and Ford Administrations by the leadership the Executive Branch gave to the matter of grant reform. President Ford, many of my colleagues will recall, impressed on the country the importance of this agenda by the use of what he called "Mess Charts." We still have some copies of those around. They showed dramatically the incredible complexity of the inter-relationships in the Federal grants-in-aid system.

Unfortunately, the last administration, under President Carter, did not contribute much to the improvement of the Federal intergovernmental aid system. In fact, the mess grew worse under Carter. Many Federal programs were further categorized and fragmented. Numerous small new programs were created and funded for the first time, especially in the field of education. In other areas, such as manpower and community development, past program consolidations were partially undermined as new categorical grants were put in place and categories were carved out within the broader grants.

THE BLAME IS SHARED

We are all to blame for the current state of the Federal system—Congress, Executive Branch Officials, Federal Bureaucrats, State and Local officials, and interest groups. The disarray in the system has been created through piecemeal responses to perceived problems. Congress, Governors, and Mayors have attempted to be responsive to the needs of their constituents by promoting specific programs to serve those needs. In fact, we seem to have been operating under the philosophy that "for every problem there should be a Federal program," or better yet, several programs! State and local governments have, for the most part, been unwilling to oppose the Federal intrusion for fear of losing needed Federal funds. The whole system has spawned a new breed of fat cats known as the "Beltway Bandits"—consultants and experts who encircle Washington to help State and local governments and private recipients and prospective recipients of Federal aid funds cut through the red tape and get the information they need to tap these Federal spigots. These special interest groups have been responsible for the "care and feeding" of these programs, as the ACIR so aptly puts it.

The net result is the hundreds of Federal grants-in-aid programs now on the books. Many of them are quite small. The public purpose is unclear in many of them. The impact on the problems towards which these programs are directed is infinitesimal in many cases. However, their cumulative cost is quite large and their impact on the governmental system quite destructive.

PROGRESS IN 1981

Fortunately, the Omnibus Reconciliation Act of 1981 provided some much-needed movement on program consolidation, administrative simplification and increased State and local flexibilities on the use of Federal grant funds in a

number of program areas. The 8 block grants contained in the Reconciliation Act took us several giant steps in the right direction. However, I think it is fair to say that no one in this room is, or should be, completely satisfied with the new legislation. Some of the Reconciliation provisions are block grants in name only—they don't do much consolidating and they don't give the States sufficient flexibility to provide services in the most rational and responsive ways. We need further action to streamline and rationalize the Federal grant system so as to improve intergovernmental relationships and enhance the efficiency with which scarce tax dollars are used.

My staff has prepared a summary of the major block grant provisions of the Reconciliation Act, compared with the original proposals of President Reagan. This summary is attached to my prepared statement. I believe it may be of use to the subcommittee.

I think it is vitally important that we take sufficient time in developing the "next steps" in grant reform to "let the dust settle" from the changes made in the Reconciliation Act. If we keep things continually disrupted by frequent changes in law and regulations, we may sow seeds of confusion and inefficiency and poor decisions on priorities that will cause grant consolidation and simplification to be declared a failure before it has really had a chance to work. Today's hearing and the other work this subcommittee is doing are important parts of the needed reasoned consideration of "next steps."

PROPOSED "MEGABLOCK" EXPERIMENTS

Today, I want to propose to the Subcommittee and the Governors that you consider a further important step in program consolidation and increase flexibility for the States. I call the idea I want to describe briefly the "megablock." The "megablock" as I visualize it would be a *State-designed* consolidation of Federal funding and programs. The Federal Government could invite a limited number of States—perhaps eight or ten—to propose a package of programs to be consolidated on a trial basis. One group of states might propose, for example, to pool Federal and State funding for AFDC, Food Stamps, Medicaid, Social Services and perhaps other programs into a single, integrated state plan for meeting financial, health care and social service needs of low-income people. Other states might propose megablocks in the fields of education, housing, community development, and transportation, etc.

The key point is that we should test out a variety of comprehensive program consolidation options without undertaking them on a nationwide basis all at once. I am convinced that had the Nixon administration proposed major statewide demonstrations of some of its New Federalism concepts in the early 1970s, we would be much farther down the road to grant reform than we are today.

States receiving megablocks would be free to spell out the details of how the programs would operate, subject only to some minimal Federal criteria. For instance it would be appropriate—and probably a prerequisite for starting such experiments—that States be required to demonstrate that they would have safeguards in place to assure equitable distribution of benefits under the consolidated program to all citizens who stand in equal need.

It would also be essential, of course, to provide standards and evaluation procedures in order to assess the relative success of the state experience and enable Congress to discharge its responsibility to monitor the use of Federal resources. These standards and procedures would need to be kept simple. They should answer four or five years down the road the simple question: "Were the Federal resources used for their intended purposes at least as effectively and efficiently as they would have been under the old categorical approach?" If that question can clearly be answered "yes," then the experiments will be successful.

I do not have available for presentation all the necessary details that would be included in a bill authorizing "megablock" experiments. If the Subcommittee and the Governors find merit in the concept, my staff and I would be delighted to work with you in taking this idea, fleshing it out, and turning it into a practical and workable plan.

My own view is that something like the concept I have described is going to be essential in making further major progress toward grant consolidation and simplification. Previous initiatives such as "integrated grants," the Joint Funding Simplification Act, and even the Governors' own proposal to "sort-out" Federal versus State roles—which I am personally supportive of—have not gained the momentum needed to cause further reform for the Federal grants-in-

aid system. It is time for us to think about making substantial progress through approaches such as the "megablock." We must take every available avenue of progress that we can find to decongest our overloaded intergovernmental system.

Mr. Chairman, I would like to commend you, other members of the subcommittee, and the Governors for grappling with the important issue of grant reform. I would also like to thank you for listening to my proposal this morning. I look forward to the continuing dialogue on these subjects. I pledge to you my cooperation and offer to you the potential of using the budget process to help achieve further movement on these issues.

SUMMARIES OF BLOCK GRANT PROVISIONS OF 1981 OMNIBUS RECONCILIATION ACT

EDUCATION CONSOLIDATION AND IMPROVEMENT ACT OF 1981

Program features	President's proposal	Reconciliation action
Programs consolidated	45 programs: Chapter I consolidates titles I and VI of Elementary and Secondary Education Act (ESEA). Chapter II consolidates titles II, III, IV, V, VIII, and IX of ESEA; plus teacher corps, teacher centers, science teacher training, civil rights training, alcohol and drug abuse education follow-through, handicapped education, and career education.	33 programs total: Chapter I consolidates title I of ESEA. Chapter II consolidates titles II, III, IV, V, VI, VII, and IX (except part c) of ESEA; teacher corps, teacher centers, science teacher training, alcohol and drug abuse education follow-through. Chapter III: general provisions.
Recipient	Chapter I: State Education Agency (SEA) 13 percent; Local Education Agency (LEA) 87 percent. Chapter II: SEA.	Chapter I: SEA (1 percent administrative cap) and LEA. Chapter II: SEA with 80 percent distributed to LEA.
Authorized services	Those of programs consolidated	Those of programs consolidated.
Authorization	$4.563 billion in fiscal year 1982; $4.809 billion in fiscal year 1983; $5.053 billion in fiscal year 1984.	Chapter I: $3.480 billion in fiscal year 1982 through fiscal year 1984. (Reconciliation reduction below prior policies: Fiscal year 1982—$38 million; fiscal year 1983—$367 million; fiscal year 1984—$769 million). Chapter II: $589 million for fiscal year 1982 through fiscal year 1984. (Reconciliation reduction below prior policies: Fiscal year 1982—$15 million; fiscal year 1983—$140 million; fiscal year 1984—$235 million.)
Provisions	Chapter I: Annual intended use State plan, 1-time LEA transition plan. Chapter II: Annual intended use State plan.	Chapter I: LEA intended use application for SEA approval at least once every 3 years, LEA maintenance of effort requirement at 90 percent, supplement not supplant and comparability of services. Chapter II: SEA intended use application to Secretary of Education at least once every 3 years. Effective date Oct. 1, 1982. (Title XVII transition provisions do not apply.)

COMMUNITY SERVICES BLOCK GRANT

Programs consolidated [1]	Community services programs (community action agencies and local government and nonprofit agencies serving migrant and seasonal farmworkers).
Recipient	State.
Authorized services	Those of programs consolidated (90 percent of funds must go to existing community action agencies in fiscal year 1982).
Authorization	$354 million in fiscal year 1982 through 1986. No State match required. $35 million for special HHS projects (reconciliation reduction below prior policies: Fiscal year 1982—$118 million; fiscal year 1983—$220 million; fiscal year 1984—$250 million).
Provisions	Termination of CSA; establishes an Office of Community Services in HHS; annual application with public hearings after 1st year. Effective date Oct. 1, 1982 (1st year transition provision allows optional State participation).

Footnotes at end of table.

SUMMARIES OF BLOCK GRANT PROVISIONS OF 1981 OMNIBUS RECONCILIATION ACT—Continued

SOCIAL SERVICES BLOCK GRANT

Program features	President's proposal	Reconciliation action
Programs consolidated	10 programs: Title XX social services, training and day care adoption assistance, foster care, and child welfare, runaway youth, child abuse, rehabilitation services, juvenile justice, developmental disabilities and community services administration (CSA).	2 programs: Title XX social services and training and day care.
Recipient	State	State.
Authorized services	Those of programs consolidated	Those of programs consolidated.
Authorization	$3.8 billion for fiscal year 1982 through 1985. No State match required, 10 percent may be used for other HHS block grants.	$2.4 billion in fiscal year 1982; $2.45 billion in fiscal year 1983; $2.5 billion in fiscal year 1984; $2.6 billion in fiscal year 1985; $2.7 billion in fiscal year 1986 and succeeding fiscal years. No State match required. 10 percent may be used for other HHS block grants. (Reconciliation reductions below prior policies: fiscal year 1982—$699 million; fiscal year 1983—$755 million; fiscal year 1984—$812 million.)
Provisions	Annual intended use report with public hearing; biennial independent audit. Effective date Oct. 1, 1981.	Annual intended use report with public hearing; biennial independent audit. Effective date Oct. 1, 1981 (title XVII provisions do not apply).

ALCOHOL, DRUG ABUSE AND MENTAL HEALTH SERVICES BLOCK GRANT

Programs consolidated[2]	5 programs: Drug abuse project and formula grants, alcohol project and formula grants, and community mental health centers.
Recipient	State.
Authorized services	Those of programs consolidated with 35 percent set-aside each for alcohol abuse and drug abuse; mental health centers same proportion of funding in fiscal year 1982 with 5 percent cut allowed in fiscal year 1983 and 15 percent in fiscal year 1984.
Authorization	$491 million in fiscal year 1982, $511 million in fiscal year 1983, $532 million in fiscal year 1984. No State match required. 7 percent may be used for other HHS block grants. (Reconciliation reduction below prior policies: fiscal year 1982—$67 million; fiscal year 1983—$174 million; fiscal year 1984—$225 million.)
Provisions	Annual intended use report with public hearings; annual independent audits. Effective date Oct. 1, 1981. (Title XVI audit provisions do not apply; title XVII transition provisions do apply.)

PRIMARY CARE BLOCK GRANT

Programs consolidated[3]	1 program: Community health centers.
Recipient	State.
Authorized services	Those of current program.
Authorization	$2.5 million in fiscal year 1982 for planning grants to States (no State grant shall exceed $150,000),[4] $303 million in fiscal year 1983 and $327 million in fiscal year 1984. (Reconciliation reduction below prior policies: fiscal year 1982—$23 million; fiscal year 1983—$58 million; fiscal year 1984—$69 million.)
Provisions	Annual application with public hearings after the 1st year; annual independent audit. Effective date Oct. 1, 1982. (Title XVII transition provisions do not apply.)

Footnotes at end of table.

SUMMARIES OF BLOCK GRANT PROVISIONS OF 1981 OMNIBUS RECONCILIATION ACT—Continued

MATERNAL AND CHILD HEALTH BLOCK GRANT

Program features	President's proposal	Reconciliation action
Programs consolidated[5]	7 programs: Maternal and child health grants, hemophilia, lead paint poisoning prevention, adolescent pregnancy, sudden infant death syndrome and supplemental security income for disabled children.	
Recipient	State.	
Authorized services	Those of programs consolidated.	
Authorization	$373 million in fiscal year 1982 through 1984. State match 75 cents for each Federal dollar. (Reconciliation reduction below prior policies: fiscal year 1982 $41 million; fiscal year 1983—$112 million, fiscal year 1984—$157 million.)	
Provisions	Annual intended use report; annual report on activities; biennial independent audit. Effective date Oct. 1, 1981. (Title XVII provisions do not apply.)	

PREVENTIVE HEALTH AND HEALTH SERVICES BLOCK GRANT

Programs consolidated[6]	8 programs in Preventive Health Services: Health incentive grants, high blood pressure, risk reduction and health education, fluoridation, rat control, venereal disease, family planning and adolescent health (the latter was included as an optional service under the maternal and child health care block grant in reconciliation). 15 programs in Health Services: Primary health care centers, primary health care R. & D., home health services, emergency medical services, mental health services, drug abuse project grants and contracts, drug abuse formula grants, alcohol project grants and contracts, alcohol formula grants, black lung services, migrant health, maternal and child health, SSI children, hemophilia services and sudden infant death syndrome (the latter 6 programs remained separate categorical programs; primary health care, mental health and drug abuse and maternal and child health were consolidated in 3 other block grants).	8 programs: Health incentive grants, high blood pressure, risk reduction and health education, fluoridation, rat control, home health services, emergency medical services and rape crisis centers.
Recipient	State	State.
Authorized Services	Those of programs consolidated	Those of programs consolidated with set aside in fiscal year 1982 for emergency medical services and in fiscal year 1982 through fiscal year 1984 for hypertension and rape crisis centers.
Authorization	Preventive Health Services: $242 million for 1982 through 1985. Health Services: $1.138 billion annually for 1982 through 1985. Both grants specify: No State match required. 10 percent may be used for other HHS block grants.	$95 million in fiscal year 1982, $97 million in fiscal year 1983, $99 million in fiscal year 1984. No State match required. 7 percent may be used for other HHS block grants. (Reconciliation reductions below prior policies: fiscal year 1982—$11 million; fiscal year 1983—$29 million; fiscal year 1984—$40 million.)
Provisions	Both grants require: Annual intended use report; biennial State activities report and independent audit, Effective date Oct. 1, 1981.	Annual application with public hearings after 1st year; annual independent audit. Effective date Oct. 1, 1981. (Title XVII audit provisions do not apply.)

Footnotes at end of table.

SUMMARIES OF BLOCK GRANT PROVISIONS OF 1981 OMNIBUS RECONCILIATION ACT—Continued

LOW INCOME HOME ENERGY ASSISTANCE BLOCK GRANT

Program features	President's proposal	Reconciliation action
Programs consolidated	2 programs: Low-income energy assistance and AFDC emergency energy assistance.	Low-income fuel assistance.
Recipient	State	State.
Authorized services	Those of programs consolidated	Those of the current program (85 percent to low-income households for home energy costs; 15 percent for low cost weatherization).
Authorization	$1.399 billion in fiscal year 1982 through 1985.	$1.875 billion in fiscal year 1982 through fiscal year 1984. No State match required. 10 percent may be used for other HHS block grants. (Reconciliation reduction below prior policies: fiscal year 1982—$372 million; fiscal year 1983—$672 million; fiscal year 1984—$992 million.)
Provisions	No application; biennial independent audit. Effective date Oct. 1, 1981.	Annual application with public hearing after 1st year; annual independent audit. Effective date Oct. 1, 1981. (Title XVII provisions do not apply.)

[1] Community Services Administration was included for consolidation as part of the President's Social Services Block Grant proposal.
[2] The 5 programs were included for consolidation as part of the President's Health Services Block Grant proposal.
[3] Primary health care centers and primary health care R. & D. were included for consolidation as part of the President's Health Services Block Grant proposal.
[4] In fiscal year 1982 the program will continue as a Federal categorical program with an authorization of $284 million.
[5] The 7 programs were included for consolidation as part of the President's Health Services Block Grant proposal.
[6] Preventive Health Services and Health Services were consolidated as 2 separate block grants under the President's proposal.

Senator DURENBERGER. Jack Danforth has no opening statement. However, two members of the Committee on Governmental Affairs do have opening statements which they would like accepted for the record. They are Senator Roth, Chairman of the Committee on Governmental Affairs, and Senator Sasser.

[The opening statements of Senators Roth and Sasser follow:]

OPENING STATEMENT OF SENATOR ROTH

It has been written that by perseverance the snail reached the ark. So it seems that the advocates of grant reform move inch by inch closer to their goal of improved relations between the various levels of government in our system of American Federalism. The contours of this issue are many and varied, with problems of fragmentation, duplication, ineffectiveness, and lost accountability of primary importance. Many other concerns round out the list. But it is only through persistence in addressing these perennial issues in intergovernmental relations that we will ever see real progress made toward a more functional federalism in this nation. For this reason I am particularly pleased that Senator Durenberger is holding this block grant hearing today, building upon the solid foundation for reform established by his subcommittee to this point in the 97th Congress.

This record in combination with the work of the full Committee on Governmental Affairs and the hearings held in recent months by the House Subcommittee on Intergovernmental Relations and Human Resources provides an accurate and up to date reading of the imbalance that has developed among the governments in our system. This imbalance, which is both fiscal and programmatic in nature, is exemplified by the vast centralization of power and resources in Washington, and the concomitant erosion authority and autonomy at the State and local level.

In our newfangled federalism, officials in subnational units of government must administer inflexible, narrowly focused categorical programs, with little discretion to tailor programs to the needs as they are perceived in the individual communities. The current state of confusion, frustration, and ineffectiveness at the recipient level is directly attributable in part to this approach to service delivery.

The trend toward centralization is not new. The breakdown of the judicial and constitutional barriers to the expansion of the Federal Government which began in earnest in the 1930s bore fruit in the rapid programmatic growth of the 1960s. When administrative and coordinative problems quickly arose in this unwieldy system, the block grant concept was fixed upon as a way to simplify the grant maze. Block grants were seen as a way to distribute Federal funds in an equitable manner and with the flexibility that would permit recipients to use the funds to meet their specific needs, within the context of broad Federal guidelines.

Yet as rational as the block grant approach is, it has been little used by policy makers here in Washington. Prior to this year, only five block grants had been created, along with the single general revenue sharing program. Since their creation, these block grants have undergone a process of recategorization as administration and programmatic "strings" have been added with each successive Congress. And General Revenue Sharing, which is the most efficiently administered of all Federal grants, recently has been suggested as a target for elimination.

Now President Reagan's New Federalism Initiatives will reinforce the effort to redress the problems that we face in intergovernmental relations. I am impressed with and encouraged by this new direction, and by the strength of the Administration's commitment to keep a steady course in their efforts to return authority and resources to the State and local levels. Many have pointed to the block grants created in the recently completed reconciliation process as a significant sign of this new trend. I, too, applaud these developments, and look forward to the relaxation of tension, and reduction of confrontation that we all now observe in intergovernmental relations. Yet, I must say in candor that these changes fell short of what the President proposed, and what the governors and state legislators said that they will need to manage effectively in this period of declining resources. For example, whereas the President proposed the consolidation of some 85 categorical programs into 7 block grants, the reconciliation bill produced 9 blocks encompassing only 73 programs. Even more importantly these 9 block grants encompass only approximately $10.2 billion in FY82 budget authority, nearly $5 billion short of the $15.1 billion FY82 authority proposed initially by the President.

Patience has been defined as a minor form of despair disguised as virtue. I think that State and local officials have been very patient with a Federal system that at this point is not working very well. And in light of the funding uncertainties, and the procedures and regulations that still bind the system, I am not surprised if their patience is running low, and if their "minor despair" is escalating.

The general interest in improving intergovernmental relations evident throughout the nation today, and the caliber of the witnesses appearing before the subcommittee on this subject this morning underscore the importance of basic structural changes in this system. The consolidation of categorical grants into general purpose block grants is a primary means of bringing these changes about. The consolidation title of my grant reform bill, S. 807, and the boilerplate language for block grants that has been the subject of hearings in this subcommittee will be useful tools in focusing the attention of the Congress on these issues, and I hope that they will continue to make progress in the remaining weeks of this first session. Ultimately, today's hearing and those that follow will help to ensure that this is the outcome. For this reason I acknowledge the patient perseverance of Senator Durenberger, and the witnesses appearing before the subcommittee today as they again seek a fairer, more effective balance in our federal system.

Opening Statement of Senator Sasser

Good morning. I want to commend Chairman Durenberger for holding this hearing this morning. I also want to thank Governors Snelling, Busbee, and Matheson for appearing before the subcommittee today to discuss the experience with the new block grants that have been created pursuant to the Omnibus Reconciliation Act of 1981.

Let me say from the outset, I am very sympathetic with many of the Governors' concerns that are going to be set forth in the hearing today.

They correctly note that the first round of budget cuts fell very harshly on State and local governments. Indeed, perhaps some $12 billion of grants-in-aid cuts were contained in the Reconciliation Act.

The severity of these reductions has already caused 30 States, including my State of Tennessee, to raise State taxes by some $2.5 billion in 1981. The second round of budget cuts also proposes some reductions in very important programs like medicaid and general revenue sharing. These are unwise proposals which I think will not win the approval of the Congress.

The Governors are also rightly concerned about proposed Treasury Department policies that might end the use of industrial development bonds. Again, the administration is off the mark in proposing these measures. I am joining with a number of colleagues on both sides of the aisle to make sure that we do not curb the use of these bonds and that we get the mortgage revenue bond program for our Nation's housing industry moving again. I commend Senator Durenberger for the strong position he has also taken in this regard.

Finally, I would also like to support the recommendation of the National Governors' Association that they receive advance notice of pending changes in Federal grants-in-aid legislation. Now that is the very essence of the "fiscal note" legislation, S. 43, that Senator Durenberger and I have steered through the Governmental Affairs Committee in both the 96th and 97th Congress. This important bill, however, has yet to be signed into law. I would hope that the Governors keep up their strong support for this measure so that we can make it an integral part of the budget process and provide State and local governments with the full information they need to adjust to the cuts they are now receiving in Federal aid.

Thank you Mr. Chairman.

Senator DURENBERGER. At this point, then, we will turn to our panel of Governors. We will begin with our honored guest, the Chairman of the National Governors' Association, Governor Richard Snelling. We welcome you here.

TESTIMONY OF RICHARD A. SNELLING, GOVERNOR OF VERMONT; GEORGE BUSBEE, GOVERNOR OF GEORGIA; AND SCOTT M. MATHESON, GOVERNOR OF UTAH

Mr. SNELLING. Thank you very much, Mr. Chairman and Senators.

May I begin by telling you how much we appreciate your interest and concern in the restoration and preservation of the Federal system. Each of you has already clearly demonstrated that you are determined to help put us on a better track. But I particularly want to say to you, Mr. Chairman, that your constant leadership in this area is a source of great satisfaction to the Governors. I think I can speak for my colleagues when I say that any one of them would have been glad to make the opening statement that you made concerning the importance to this Nation of preserving the vitality of the States and of making sure that government is close enough to home to be accountable and responsive.

Mr. Chairman, Senators, there is an underlying theme to the testimony that you are going to hear today from three Governors from diverse States and from different political parties. It is the need to dispel the clouds of uncertainty that overhang the Federal system and that are hindering the ability of State and local governments to respond to what we consider to be the very appropriate challenges of President Reagan's Federalism Initiatives.

This uncertainty has several elements. I am sorry to say that the importance of that uncertainty grows day by day. As most State

governments are now entering the fifth month of their 1982 fiscal year, they do not know the final level of funding of many Federal programs which they are charged with administering. We are five-twelfths through the fiscal year. The size of support of the Federal Government is as yet unknown.

Governors are now deeply involved in preparing the budgets to propose to their legislatures for fiscal year 1983. They do not know where tens of billions of dollars in frequently talked about but totally unidentified 1983 and 1984 budget cuts will fall.

As State and local and even business leaders—and the President—have suggested, some of the responsibilities which in the past have been assigned to the Federal Government without any particular rationale should flow back down closer to the people. As businesses contemplate shrinking Federal aid and unprecedented interest rates for tax-exempt borrowing, they are concerned that public infrastructure needs which are crucial to economic growth—which the other side of the goal here, such as highway and water systems—will go unmet. And as State and local officials everywhere contemplate the deep funding cuts and limited flexibility of the current, we hope interim, block grants, they ponder just how far the block grant approach to Federal funding is worth pursuing.

We are here today not just to outline these problems but, as the past, present and future chairmen of the National Governors' Association, to recommend some fairly specific plans for attacking them that we believe will meet your concerns as well as our own.

On September 24, the day that President Reagan presented his request for additional funding cuts to the Nation, the executive committee of the National Governors' Association met and unanimously adopted a six-point statement that summarizes our concerns.

I should point out to you that under our bylaws, the membership by party is just as completely balanced as it possibly can be. So when the executive committee of our organization unanimously adopts six-point statements, it does fairly reflect the concerns of the Governors and we hope of the States of the United States.

We discussed these six points with the President that same afternoon and have already communicated them to the leaders and Members of the Congress. I would like to submit them also to you, Senator Durenberger, for the record.[1]

Our testimony today will amplify these points. But, very frankly, we count not so much on our testimony as on the opportunity we hope to have with you and the other Senators for dialog on these very important issues. In some ways this is the first opportunity that we have had with such a diverse group within the Senate to discuss matters which supposedly will mature only by an increased dialog between the Federal Government and its representatives and the State government and their representative.

But each of us is here today separately prepared to report to you on how we are implementing the block grants enacted by the Congress last year and to discuss with you the omnibus block grant requirements on which your subcommittee has been working and which we believe are essential if further progress is to be made in simplifying the Federal system.

[1] See p. 45.

With my own time I would like to discuss primarily the importance of fiscal stability toward the success of the President's program and suggest how we can achieve more fiscal stability for the States than is presently in the cards.

Governor George Busbee of Georgia, who is the past Chairman of NGA, and, as you know, was instrumental in bringing the Governors together with a united position on medicaid and a number of other elements, will focus on the management problems confronting State and local governments and how they may be further reduced by some agreements with the Federal Government on gradual but steady sorting out of Federal, State, and local responsibilities. Governor Scott Matheson of Utah, who will succeed me as Chairman, will discuss the need for greater certainty in public infrastructure programs, such as water and highways, and will briefly discuss revenue turnbacks in this context.

Mr. Chairman, with your permission, I would like to introduce for the record the rest of my statement and now speak to you about it a little less formally.

Senator DURENBERGER. Your statement will be made a part of the record and will follow the oral testimony of our other two witnesses.

Mr. SNELLING. Mr. Chairman, we all seem to agree on the problem. I would think the Nation agrees that we have twin problems, and they are quite different and yet related. The task is to solve them so that the solutions complement each other, recognizing that a failure in meeting either of the two great problems may very well impact upon the likelihood of the success of the other.

On the one hand we have to get the budget under control. All America knows that. It seems to be a point of bipartisan agreement, in the Congress and among the public.

Now, quite separately, we have not thought for a very long time about the appropriateness of the various activities of various levels of government. One might say there has been no real dialog on this subject with the kind of intensity that accompanied the Federalist Papers since the Federalist Papers 200 years ago. So we have drifted to a certain extent in the sense of opportunities—opportunities for spending, for meeting needs, for quantifying needs. Senator Domenici once referred to our tendency to quantify a need and then somehow or other to assume it wasn't terribly important at what pace we filled that need or who filled that need. So we have to do both of these, the sorting out of appropriate relationships and budget cutting.

The concern of the Governors is that up to now the budget cutting part of it has been so illogically entwined with the concepts—the intellectual concepts—of federalism as to cause many people to think that when we speak about federalism, we are talking about the need for States to make decisions about what gets funded and what does not. And on the other side of the coin, many people believe that the essential requirement of budget cutting is to turn responsibilities back to the States, which of course is totally at odds with the fundamental game plan. The game plan is to reduce the overall burden of government on the people and to make government more logical.

In the reconciliation bill, for example, State and local programs, which make up about 15 percent of the Federal budget, absorbed 33

percent of the cuts. I know from talking to the Senators here that you all agree that it is possible for this whole program to come tumbling down if it is done in such a way that it loses the support of the American people.

The dilemma seems to be that where the budget is out of control is in what is referred to as uncontrollable items. So a very illogical, and innocent, thing is happening. We are controlling the bejeepers out of the controllables and allowing the uncontrollables to go on uncontrolled.

Senator DOMENICI. You are right.

Mr. SNELLING. I do not speak about this so much as a Governor. I spent most of my life in business. If you have a budget problem because some portion of your budget has gone out of control—let's say for the purpose of argument it is manufacturing—you do not solve the problem by canceling your advertising expenditures.

What is happening now is that the focus seems to be on that part which is already closest to the people, which is already doubly and sometimes triply accountable because every cent that goes to the State and local governments has to be reconfirmed by State legislatures, by the public, and frequently also by mayors and by city councils.

We are now in a very, very severe risk of failing you, of failing the President, of failing the people, because in order to try to find a very large share of what must be cut, it is cut from the most controllable, immediate services. If we then fail to deliver the goods, if it turns out that at the levels of funding expected we cannot maintain services, and if we find that so much of the safety net which has frequently been referred to lies in our backyards but requires some assistance from the Federal Government, at some point in time people may very well come to two very wrong conclusions. No. 1, that budgets can't be cut. The Governors of the United States believe budgets can be cut and must be cut. No. 2, people may very well come to the conclusion that turning responsibilities back closer to the people doesn't work and can't work because they will not recognize that simultaneously what is happening is an unfair sharing of the fiscal burden.

Mr. Chairman, Senators, we would like to suggest that there are three ways to solve this particular problem. The severity of the problem and the urgency of it is so great that, to the extent that these solutions require rethinking by anybody of positions already stated, it may be justified.

May I refer briefly to an item in this morning's paper which says that "Hill budget writers halt awaiting a White House signal" and again remind you we are 5 months into our fiscal year. As an old football player, I call that delay of the game. There is supposed to be a penalty for that.

It is time for us to get down to brass tacks. Perhaps there are three bases upon which we could agree.

First, we need adequate revenues. If the adequate revenues aren't there, then the task on the budget cutters is just too great. Now I don't like that, if that means that anyone has to reverse priorly determined positions. But the position of the Governors and the unanimous decision of the executive committee is that we must have adequate revenues to make the rest of it work.

Second, we ought to have a consensus that what we will all do is the tough but worthwhile task of bringing the uncontrollables under control.

Third, we should stabilize the rest. I am not trying to duck, nor are the other Governors trying to duck their share of the responsibility. If you have an $800 billion budget order to magnitude and any fair and appropriate share of it is stabilized and no longer grows, then any growth in the overall economy—whether it is real growth or is driven by increased revenues or driven by inflation, whatever portion is stabilized—has contributed to a solution to the problem.

Back in March, tucked away in an administration proposal, was a statement by Mr. Stockman which I suggest might be the basis for proceeding. The statement with accompanying statistics described the forward funding levels for two different kinds of State and local appropriations: First, payments for individuals through State and local government; and second, discretionary grants to all other groups. The administration in March was forecasting a growth of about 4 percent a year on the Federal-State entitlement programs and virtually no growth in the discretionary programs.

We would like you to consider that as the basis for providing us with an opportunity to start making some plans for the rest of 1982, for 1983, and for 1984.

Basically that proposal would say we will stabilize all except the so-called entitlement programs for the States, or about $46 billion. We are saying, stabilize the so-called discretionary grants, which means that the States will absorb inflation in these programs for the next several years. We will not contribute to a Federal budgetary problem if that is the agreement reached. And with respect to the Federal-State entitlement programs, at the moment most Governors would probably settle for the Stockman recommendation of March, which was a 4-percent growth.

Governor Busbee will have some more to say about a 4-percent growth in entitlement programs in light of the kind of automatic escalators that are in place for many Federal programs.

Basically our statement to you is that, at this point in time, the only way we are going to have honest discussions about federalism is to separate it from the discussions about budget cuts. It can't be allowed to appear to the American people that what we had before where the Congress decided how to distribute increases was not federalism and now that what federalism is is where the States get to decide upon the decreases. We must separate these two.

My particular suggestion for that would be that we achieve the separation of federalism reform and budget cutting by stabilizing grants to State and local governments for the next several years so that we can get down to the very serious discussions about the shape of programs, the design of programs, the locus of programs.

Mr. Chairman, I appreciate your courtesy very much. I would like to turn the rest of the time over to my two colleagues, subject to your questions.

Senator DURENBURGER. If I may make one comment—I hesitate to do this to Governors—but, if we are going to get into a dialog on this subject, I will have to assume that the chairman of the association has

covered an awful lot of ground in approximately 20 minutes. Hopefully, both Governor Busbee and Governor Matheson will be able to abbreviate their comments so that we can get to the dialog with those whose curiosity and, I think, whose response you have certainly piqued with your statement.

Keeping that thought in mind, Governor Busbee, we would appreciate hearing from you.

Mr. BUSBEE. Thank you, Mr. Chairman.

I would like to briefly outline, if I may, for this subcommittee the problems that the States are encountering in providing effective and responsible fiscal management in a time of tremendous uncertainty in Federal-State relations.

Although nearly two-thirds of the budget cuts which were made in the Omnibus Reconciliation Act were in grants-in-aid to States and localities, and although the States are affected by the Federal tax cut package—they are affected immediately by loss of revenues—it is really not my purpose in coming here today to complain about the magnitude of the cuts and the revenue reductions that have been made. What I am here to describe to you is the overriding problem that the States have had with the Federal budget process.

As this administration entered office facing a chronically troubled economy and an ever-increasing sense of public disillusionment with government in general, the Governors—as Governor Snelling said—in a bipartisan way, supported the President and the Congress in their efforts to make a fundamental change in the very nature of American Government.

We recognized that it was imperative that the Federal budget be brought under control, and we knew that this would necessitate a lot of programmatic changes.

But despite the fact that nearly two-thirds of the budget cuts included in the Omnibus Reconciliation Act were in grants-in-aid to States and localities and were implemented by States through their budgets, there was no prior consultation by the administration with most Members of Congress nor by either the administration or Congress with the States that were affected by these cuts. As a result, we not only have a Federal budget that is not balanced, but the budgets of the States are in disarray and chaos.

As you know, many States are mandated by their constitutions to balance their budgets. Prior to this action by the administration and Congress, the budget process in State governments consisted of an orderly flow of actions beginning with preliminary revenue forecasts and identification of continuing needs of State government. The Governors received agency funding requests. We met with the budget analysts and heads of our departments and developed a budget recommendation for the legislature, including whatever improvements revenues would permit. The legislature then debated funding priorities and passed the final version of the appropriations bill.

The problem States are having in adjusting to a constantly shifting mosaic of Federal budget and tax plans is made all the more difficult and frustrating by a basic difference in Federal and State fiscal years. Forty-eight of the fifty States operate on a different fiscal year than the Federal Government. We start on July 1. This means that the dramatic changes in Federal grant funding and management and the

transfer of major program responsibilities to the States included in the Omnibus Reconciliation Act of 1981 have really gone into effect 3 months into most States' fiscal year 1982 and many months after the preparation of our State budgets for fiscal year 1982.

In November of 1980, after many weeks of preparation, I had completed my budget recommendations to the legislature for the fiscal year 1982 which began on July 1, 1981. In March of 1981, our legislature had completed the budgetary process and the budget was signed into law. What this meant was our State agencies had several months of leadtime and were able to plan for the implementation of the budget that began on July 1.

I want to call to your attention what then happened here, Mr. Chairman, in Washington, and how it affected the budget process at the State level.

In March we looked at and analyzed the President's original budget proposals. In April we poured over the House and Senate alternatives and looked up the definition of reconciliation. In May we had the budget resolution and reconciliation instructions adopted by Congress. In June our photocopying expenses really just soared as we passed out to our budget analysts the Senate and House reconciliation bills, each running well over 1,000 pages and affecting the entire landscape of Federal-State relations.

At about the same time, the administration proposed a series of rescissions and deferrals for fiscal year 1981, again changing every underlying assumption of a State budget already adopted almost a year previously. Then in July came the President's 1,000-plus page reconciliation floor substitute coupled with a plan to "cap" medicaid contributions, soon followed by the supposedly final congressional conference report.

In July and August we went through the same process of adjustment and sheer guessing with the Federal tax cut bill, portions of which would be automatically incorporated into our own State tax code.

Just as we began our budget hearings for fiscal year 1983—Scott Matheson has been in his for 4 weeks; I have been in mine for 3 weeks—we learned that the President was proposing additional cuts in largely unspecified areas for Federal fiscal year 1982 and deferrals of previously appropriated funds. In addition, I understand that the Senate is considering its own package of additional budget adjustments for fiscal year 1982. Finally, all of this current effort may prove to be moot when the administration adjusts its forecasts and economic assumptions, which will come I suppose in December.

As I have just stated, most States are now working on budgets for fiscal year 1983 with, as yet, no real certainty as to what funds will be available for the remainder of fiscal year 1982 and only the vaguest notion about new cuts in grants-in-aid, new block grants, new tax cuts or increases, or entire new areas of Government to be shifted to the States.

I would like to comment very briefly, Mr. Chairman, on the havoc that Federal budget cuts within existing State budgets cause to existing and operating programs. These cuts made at the Federal level on State budgets don't just automatically take effect. If you make cuts in our budget in midyear, the magnitude of the services that have to be

cut is doubled because we only have the remainder of a half a year to make up the total cut.

For example, if in the last quarter of the fiscal year we are told to cut $50 million from a program, in effect we have to reduce the level of services in that program by $200 million for the remainder of the quarter. Then, as we go into the next fiscal year and have an entire fiscal year to work with, we have to increase that program by $150 million to have cut $50 million. What we have is a yo-yo going up and down, with people being displaced and with programs being changed and displaced.

This problem is compounded by the fact that we have Federal restraints prohibiting us from immediately making the cuts that you tell us to impose.

For instance, take medicaid. It was necessary for me to cut $67 million out of medicaid after this fiscal year had commenced. Federal regulations required us to give a 60-day notice of the program changes needed to effectuate these cuts, which had to be accomplished during only a portion of the fiscal year. Add to the 60-day notice the other bureaucratic notice requirements, and we have to provide a minimum of 90 days leadtime before implementing the cuts. If you start in January, you are going to be in March before you can even put them in place. Five States have been enjoined by the courts from making the cuts even after this period of time has expired.

Much has been said about the block grants and the latitude given to the States for making the cuts. But as Senator Domenici points out in his statement, these are really block grants in name only.

During the entire debate in Congress, all of us sat back knowing what the cuts would total, but all we could do was speculate on what latitude we would have after some of the categorical programs were combined into block grants. We could not react with our State budgets even though we knew what the budget cuts would be, unless we knew what latitude we would have in the block grant area.

The States have long maintained that with increased flexibility we could manage Federal programs more efficiently and more responsively. Initially, block grants appeared to hold considerable promise as a method to provide Governors with this flexibility. The reality of block grants, however, has not lived up to that promise.

I am going to give you one example to demonstrate what Senator Domenici refers to as block grants in name only.

Of the 500 categorical grants he refers to, we have only 57 combined in the block grants. Thirty-three programs are combined into the elementary and secondary education grant and 9 programs go into preventive health block grant. If you eliminate these two block grants, you can see that only 15 out of 500 categorical programs are covered in the other block grants.

Even with these few flexible grants that were given to us, many restrictions remain. For example, we can transfer 7 percent from health prevention block grants, but then we are limited to where we can transfer it to the alcohol grant, the primary care grant, or the maternal and child health grant. However, we can only transfer 3 percent in the first 9 months and the remaining 4 percent in the last 3 months.

So last week I did this: I applied this great block grant and found that in this State's fiscal year I have the flexibility to redirect $91,530 out of an available $3,051,000.

I will not go into the additional examples. Just adopt them, if you would, for the record. I have tried to outline some of the problems that we are experiencing at the State level and our difficulty in balancing the State budget.

I want to make it infinitely clear that all of the Governors are aware of the enormous task which this Congress and this administration are facing. We are aware of the fact that the necessary action cannot be taken to address our national economic ills according to some precisely prearranged timetable. Some uncertainty is inevitable. We are going to do the best we can at the State level and under the circumstances we find ourselves in today.

However, I come before you today and I plead with you to consider the one proposal that I am about to make. I suggest to you, Mr. Chairman, and other members of this subcommittee, that these problems which are being passed down to the States are unavoidably your problems, the President's problems, and the country's problems, just like the economic ills of this Nation are the Governors' problems.

In the next few years, if the Federal budget is ever to be balanced, Congress and the administration will have to take on a major attempt to control the burgeoning cost of entitlement programs, several of which—particularly medicaid and welfare—the States share responsibility for financing and managing. This effort will require very close consultation and coordination between the States and the Federal Government or it is going to fail, Mr. Chairman, because, unfortunately, controlling the actual cost of a program out in the field is not simply a matter of drafting and fine tuning some budget figures.

I strongly believe that the States can and will serve a vital role in helping to balance the Federal budget and in assuming a variety of responsibilities that were previously performed at the Federal level. But we can do nothing but react, and react only on a piecemeal basis, if no long-term plan is adopted with full consultation of everyone involved and then kept in place long enough to give us a chance to make it work.

To date, there has been no true prior consultation with the Governors by the administration on the New Federalism and on budget cuts. I will say I credit Rich Williamson and his staff at the White House for making a yeoman's effort. Unfortunately, too many in the administration view consultation as an after-the-fact briefing; or we get briefed 3 hours before proposals are sent up to Congress.

Now, many Members of Congress have listened to our concerns and recommendations—like Bob Dole on medicaid, members of this subcommittee on block grants, and Senators Domenici, Nunn, and Mattingly on important issues like wastewater treatment.

I think that you must have noted the bipartisan nature of the Governors' concerns and suggestions throughout the past year and even today. As I say, we are not here to whine or beg. We are here to say we understand the complexity of your task and we do understand what our respective and collective constituents want and what are their concerns.

We share with you the desire to balance the Federal budget, and the long overdue need to eliminate waste at every level. But, Mr. Chairman and members of this subcommittee, this cannot be accomplished in a vacuum. I think it is time that we had a domestic economic summit involving the President, the bipartisan leadership of the Congress, and our leadership; so that we might gain general agreement on the ultimate prime responsibilities for Government programs, the budget targets we should all plan for, and the time frame in which we are going to reach those goals.

The mood of this Congress and the mood of the people is to balance the Federal budget and to curtail Federal programs. The members of this subcommittee, Congress as a whole, and this administration know that we are talking about $80 to $100 billion in unidentified cuts which will have to be made if we are going to balance the Federal budget in 1984–85. This is an enormous responsibility. I sit here today on behalf of the Governors and I pledge to this subcommittee, Congress and the administration that we will do our part if we are given the opportunity to participate.

Thank you very much, Mr. Chairman.

Senator DURENBERGER. Let me just say briefly, for the record in particular, that no one has the impression that you are here, after the fact, telling us about our mistakes. I would like to compliment you when, in your capacity as Chairman of the Association, you spent all of those months—February, March, April, May, June, July—not at your own photocopying machine but here trying to alert us, ahead of time, of some of these problems and trying to do your own very bipartisan summitry which we were going through in this process. I am sure we appreciate it, even though it may seem to you to have been somewhat of a futile effort.

Governor Matheson, welcome.

Mr. MATHESON. Thank you, Mr. Chairman.

Senator DOMENICI. Mr. Chairman, could I ask one question? What is the $91,000 that you had flexibility on versus how many millions?

Mr. BUSBEE. Three million eight-some-odd thousand dollars.

Senator DOMENICI. Thank you.

Mr. MATHESON. Mr. Chairman, members of the subcommittee, I would like to offer my written testimony for the record. I will summarize it very briefly.

Senator DURENBERGER. It will be made part of the record following that of Governors Snelling and Busbee.

Mr. MATHESON. I am very anxious to have our dialog commence.

This particular subcommittee becomes more and more important in the process, in the Federal Congress, in view of the fact that New Federalism has descended upon us in rich abundance. However, we in the States think it is descending a little unequally. The only way we are ever going to work out this sorting out and resolve some of the basic concerns which Governors Snelling and Busbee have mentioned is to work through the intergovernmental process.

I have just gone through an interesting experience as Governor of my State. I handle all of the budget hearings myself. I spent a solid month having all of my department heads and others tell me what they need next year. We are still attempting to find a way to absorb the cuts which already have occurred this year in the Congress.

One of the interesting aspects of that budget experience—among all of our frustrations and the lawsuits which descend on us when we don't appropriate necessary funds—is this: Every year in our State we cut back a little bit of capital dollars on our investment in the future. We wait 1 more year before we fix up the present. We wait another year before we invest the necessary dollars needed for our road system. I saw that as a pattern creeping through the budget process. Suddenly I decided I would expand my thinking and take a look at it from the national perspective and how it fits into the administration's economic recovery plan. I find that it is a very important component.

As I examine the public stock and its infrastructure in the country today, I suddenly see a seriously worsening condition. It is something that will have to be addressed as a part of budget balancing and economic recovery. We have ignored it as each State has done—taking 1 more year to pay the M. & L. and not investing in the future.

That is the point which I want to touch on briefly today. I spend most of my time in the Governors' Association as the chairman of the Water Subcommittee. We were concerned with building sewers. We now have a need backlog of $120 billion. We can't afford to put $120 billion into sewers. We have to make a reasonable commitment to get the basic sewage treatment facilities in place as a part of the public infrastructure, or private investment will not improve in those areas. Business does not come to communities which don't have good sewers. That is a basic fact we have to take into consideration.

I did an examination of a booklet prepared by the Council of State Planning. I also read the article in Business Week a couple of weeks ago where you were quoted, Mr. Chairman. This is a quotation which I think sums it up quite well.

> So serious is the decay of the Nation's infrastructure and so poor the prospects for its refurbishment that many sophisticated businessmen and economists believe the U.S. is entering a period of severe crisis for State and local governments. It is perfectly true that the private sector has carried the responsibility for economic growth throughout the history of the Nation. But, at virtually every stage of the Nation's history, growth was dependent on the balance between private and public investment.

Let me give a couple of examples. The interstate highways—one out of every 4 miles is now beyond the point of a service life. Thirteen percent of the bridges are now defective. Just the costs of rehabilitating and reconstructing nonurban highways to maintain existing levels will exceed $700 billion in the eighties.

I have already mentioned the water treatment needs. I was examining the problem of jails and prisons and noticed that the Attorney General's task force recommended $2 billion for new prison facilities because that infrastructure has decayed. I noticed when the President gave his speech in New Orleans he did not mention the capital infrastructure problem.

One out of every five bridges in the country requires major rehabilitation. Municipal water supply requirements are between $75 and $110 billion. These are not isolated or extreme examples. Our public works are simply wearing out.

We have played catch-up too long. We have found that that is a vital and economic part of the administration's efforts to turn around the economy.

So my suggestion is that, as a part of the New Federalism and the economic recovery proposals from this administration, we go back to the basics. We should realize that economic vitality is dependent, at least up to a material point, on investment in the public infrastructure of this country.

We are doing it on a bailing wire basis. It seems to me that we have to plug that into the equation. I want to make that the center point of my comments today. I think it hasn't been discussed openly and intelligently. Most people set it on the back burner too often. I am afraid it has now caught up with us in our economic plight.

The leadership, in examining that issue, will need to take some bold steps. I have done an interesting thing in my State. This is the first year I have done a capital budget. I have everyone in the State government so worried they will lose capital dollars that they just don't know what to think next. I have found, if you do a capital budget and look at that issue, you can find ways to meet the need. You can also find ways to save tremendous capital investment.

I suggest that that might not be a bad idea for the Federal Congress and the administration to look at. Traditionally the Congress has funded the capital dollars and the executive branch has never prepared a capital budget. I think it is time we look at that as part of the economic recovery plan.

Thank you.

Senator DURENBERGER. Thank you very much, Governor. Thanks to all three of you.

With all due respect for the three members of the subcommittee present and in order to initiate our dialog, I will turn to the Chairman of the Budget Committee and ask him to be the first to react to your comments, with either comments of his own or questions to the Governors. Then we will go through the members of the subcommittee for their questions and comments.

Pete?

Senator DOMENICI. Thank you very much, Mr. Chairman. I won't take much time. I think the Governors have given this subcommittee and the Congress some real food for thought. I hope the administration is listening also. I don't know if they have any representatives here, but I think they should listen to what is said here.

Let me ask, Governor Snelling, when you talked about stabilizing—in referring to a March statement of Mr. Stockman—did you indicate that you would recommend a cap on appropriated domestic programs, or did you indicate that it would be a cap plus something?

Mr. SNELLING. Basically what I was indicating was that we think there ought to be some comparability between the way the Federal Government treats Federal entitlement programs and the way it treats State entitlement programs. The Stockman memo listed $46 billion for discretionary grants. We suggest that might be capped for a period into the future.

With respect to the so-called entitlement items, we think we should ask ourselves what difference there is in terms of the impact on the public between, let's say, medicare, which is a Federal program, and medicaid, a shared Federal-State program. If the degree of growth that is proper in one of these is 8 percent, then probably that ought to

be taken into consideration in setting the degree of inflation absorption on the other.

My suggestion is that, with respect to these two budgetary areas, if one of them—that is, the discretionary area—were capped, it would be possible to proceed with a discussion about sorting out and a discussion about block grants. With respect to entitlements what needs to be discussed is how much protection against inflation is required, whether at the Federal or at the State level.

Senator DOMENICI. Two of you have appropriately addressed the uncontrollables or the entitlements. You, as most people who understand the budget, admonish us. I hope you understand that, when you start talking about national entitlements, about 45 percent of the basic pot of national entitlements—not counting interests costs—is social security. Another big chunk of it is medicare. That is almost $50 billion now.

I hate to put you on the spot, but you all put us on it. When you talk about controlling uncontrollables, are you talking about social security reform that would share benefits, build its reserves and thus cut the deficits, or not?

Mr. SNELLING. The Governors don't have an official position so we must each speak as honestly as we can for ourselves.

I think the 80–20 rule, or some version of it, must apply to the Federal Congress as well. If some item is a very large part of the problem, then even a relatively small correction in that area would yield a very large number of dollars. If the largest item in the budget grew by 1 or 2 percent less than it otherwise would grow, enormous changes would be made.

I don't personally see, just as an aside, how we are going to solve the problem without opening our eyes to all of the elements which are a part of it. If you were to ask me personally whether I think America would be happier with restraint where the kind of restraint was that something which is presently tied to an automatic escalator of "x" percent had a slightly smaller escalator but nevertheless some stability, some sense of expectation; or whether America would be happier with total uncertainty about what the shape of our budgets is going to be like in the future, I would opt for a fairly uniform, even-handed readjustment of any program which is admittedly out of control.

Mr. BUSBEE. Mr. Chairman, I would like to respond to this if I might. I think this is the heart of the matter. We don't agree with the terminology of uncontrollables which you referred to, Senator, at the national level. Let me point out why.

At the present time I am writing a budget. We had planned a 4-percent cost-of-living increase for retired State employees. As a result of all your cuts, we've reduced that figure to 3 percent—we have 3 percent going to retired schoolteachers.

Now when you tell me that I am not going to be able to maintain even that level this next year because of action taken here in Washington, and that I am not going to be able to give State employees my recommendation of about 5 percent—in these times of high inflation rates—because all your budget cuts have fallen on "controllable" grants-in-aid, then you obviously have an inequitable situation. I think it is wrong for the military, the social security recipients, and your

Federal employees to have built in what you call "uncontrollable" cost-of-living increases while you expect us to take it out on people who have taught for 30 years in our school system. I also think it is wrong for the Federal Government to insist that we hold cost-of-living increases for State employees to 4 or 5 percent while Federal employees are paid at a scale almost double in many instances what we can pay.

So I say, don't just look at the "controllables" in the Federal budget. Look at the "uncontrollables" and control them. I think we all have an obligation to work in this area. We need to get going, Senator Domenici, on this summit that I spoke of, because we honestly share your concern. We have said repeatedly to the President, that we will take the cuts, just give us a little discretion. We want to help you bring the budget under control, but we need to get all the relevant parties together and develop a common plan.

I remember the time we couldn't agree on a National Highway Act back about 1976 or 1977. We got the Secretary, the department heads from about five State transportation offices, the New York Port Authority, and the Miami Transit Authority. We put them on the second floor of a hotel on a remote island off of Georgia and we worked it all out. We had a fish fry when we got through. [Laughter.]

I just think, if we could get the people involved in this ball game together at a single place and time, we will have that fish fry one day. I really do.

Senator DOMENICI. Mr. Chairman, I am taking too much time. I am supposed to be with our chairman in the Environment and Public Works Committee. I believe that the makeup of the Federal budget, and what is happening to it, is part of your business here. Without considering what is happening to it, there isn't any way to address the issue of block grants or consolidation, because you run full blush into the uncontrollables. You are not going to get the kind of support that you need from the mayors and Governors, because if we don't control the entitlements, then those blocks are a farce. You will be smart enough to say what you are doing to us is making it easier to cut all of these things. You have it all in one package. You get the block out there and you can whack it 15 percent and let the other things go.

I will give you some round numbers, Governor. I don't like uncontrollables any more than you, but it is a reality. It is merely a definition that means a program which will spend out automatically, as contrasted with a program which is subject to an appropriations bill—which can, indeed on an annual basis, control the level of spending. But that is all it is.

If you want some interesting facts—when John Kennedy came into office, not so long ago, there wasn't a single American program that had a cost-of-living index automatically attached. Not a one. That has all happened since that time. Entitlements plus interest on the debt is 56 percent of the budget. Most entitlements will grow at about 10 percent a year, even under fairly optimistic economic assumptions.

The programs you are talking about here are almost all on a negative growth path. When we finish the process, they will definitely be capped and will be experiencing negative real growth. So it does appear to me that it serves a useful purpose for you to tell us that you understand the problem and are willing to bite the bullet with us.

When you speak of cutting entitlements, it is a nice thing to throw it out, but you are basically talking about social security and Federal pensions of all types. Let's talk about those—that is, the veterans and the Federal retirees. You take those three together and you have over 50 percent of the entitlements right off. Then you have medicare. Then you have medicaid.

You all may be willing to cut medicaid, but talk to Members in the other body about capping medicare, changing its formula, and you know what we got. We got a piddling little cut. Medicare is going to grow, we think, at over 15 percent a year after the cuts. In fact, medicare could grow at 19 or 20 percent a year after the reforms in the reconciliation package.

Those are the kinds of numbers we have to deal with in terms of trying to control some things.

One last comment about your notion of block grants, Governor, and how good they are and how much you support them. I think you are preaching to the choir here. Even though Sam is not on the majority party, I believe he supports the notion of block grants. So you are preaching to the choir.

Let me tell you that there is less than a consensus in the U.S. House of Representatives about block grants—far less than consensus. If you wonder where those little omnibus reconciliation grants come from—consolidations—then look at what came out versus what passed the Senate. It is considerably different. There is only one intervening step and that was a conference with the House. You look at where we didn't get them and it is where they didn't pass them.

I am not trying to lay blame, but basically there is still very strong opposition in this Congress to block granting programs. So I don't think you ought to assume that is an easy proposition to get through. It is a very difficult one.

Thank you, Mr. Chairman.

Senator DURENBERGER. Senator Nunn, if you want to make a comment on the entitlements, please do so. We seem to be making that point. Then we will switch to some limited subjects. Please go ahead.

Senator NUNN. I just want to say to the Governors that Congress and the administration have not addressed the entitlements' index in a very courageous way. What we have now done is indexed taxes, which means that you have spending indexed upward and taxes indexed on a frozen basis. This means that you haven't seen anything yet when it comes to the deficits.

When you start looking at the deficits—and I know Pete Domenici knows this better than anyone—in 1984, 1985, 1986, and 1987, you are talking about not $50, $60, and $70 billion. You are talking about $150, $200, and $250 billion. It is the most incredible display of fiscal irresponsibility I have ever witnessed—to not address the indexing on spending programs and then to index taxes. It is an incredible lack of not only economic analysis but also of simple arithmetic. But that is what has happened.

The Senate, on one occasion, passed an adjustment on the indexing formula. I think Pete Domenici in his Budget Committee came out with it. It passed. It got kicked out in the conference committee. The administration has incredibly opposed doing anything about index-

ing. That is one of those things that is frozen. That is why the administration has $80 to $100 billion in unidentified cuts. They don't know where they are going to cut. They have no earthly idea where they are going to cut. Senator Domenici is trying to put together a package that could be supported on a bipartisan basis. Every time he goes to the White House he gets turned down. There are some people living in a dream world economically.

All I am saying is I agree with all of the problems you described here today. But you ain't seen nothing yet, unless a change is made, because the deficits are really going to roll.

I also want to say to Governor Busbee that I completely agree with your call for an economic summit conference. I think it is long overdue. Several of us proposed that to the Reagan administration back before the tax cut. It was apparent, before the tax cut, that the Federal Reserve was not going to accommodate the size of the tax cut it provided. It was apparent we had a clash between fiscal and monetary policy. The only thing that was going to get interest rates down was a recession. This has been apparent for 7 or 8 months.

We haven't heard anything yet on that proposal. The administration hasn't even replied. So all I would say is I hope you get a better response to your call for an economic summit than we got from ours.

You are absolutely right. We face total chaos at the State and local level. We face tremendous problems at the national level with the overall economy.

Senator DURENBERGER. Don't you have any sense of summitry sitting in this room, right now, Sam? [Laughter.]

Senator NUNN. I think this would be a good place for it. I suggest they lock all the doors; get the President in here with his top advisers, the bipartisan group of Congressmen and leadership, the Governors and the Chairman of the Federal Reserve; shovel in food; and not let the doors open until we come out with some kind of consensus.

Senator DURENBERGER. Thank you.

Senator Mattingly, do you have any comments?

Senator MATTINGLY. I agree with what Pete was saying as well as with Sam's comments. There has been legislation offered on controlling entitlements. Senator Symms and I have already offered legislation to change the CPI and to move the COLA. Sometimes it is hard to find people to introduce legislation. I don't say they lack political courage. I will just say that they have some innate fear that something is going to happen.

But you are absolutely right, that unless entitlement programs are approached—and that was my feeling also. Senator Domenici has taken the legislation under consideration in the Budget Committee. I think that, in order to structure a fundamental reform in this country, this is what has to be approached and voted on and passed.

In order to make that happen, sometimes it is rather difficult to get 1 more than 50 here to support such a change in entitlement programs. If the Governors would also come forth and endorse not necessarily my legislation but similar types of legislation for controlling the entitlements, along with dispensing this knowledge through these hallowed halls, we could get support; and I think we could get the support immediately. It is now time for the structuring together of fundamental reform, and maybe projecting it out over a 90-day period of

time so you may come up with your plan. Basically all three of you have said pretty much the same thing. Time is needed to restore economic vitality, to do something with entitlements, to get adequate revenues moving in the State, and to get a consensus from everybody.

It returns back, though, to the uncontrollables which impact you. I would just like to say that I don't think now is the time to panic. I think now is the time to say "Yes, I am for changing the index of our country. Yes, we are for changing the entitlements." Then talk to your own legislators and get them to support this. I think that can happen. I think that is the underlying problem of this whole budget process and your problems in the State.

Senator DURENBERGER. We clearly have the message about the Federal budget. All of you know from previous hearings that the chairman of this subcommittee, and the subcommittee itself, understands you can only beat on an $85 billion pipeline so long before it starts springing leaks all over the place. That is what we have been doing for the last 8 or 9 months—trying to get the same kind of message to the administration and to our colleagues.

Let's turn to the whole issue of the so-called uncontrollables and the entitlements. Let me ask each of you about that portion, which Governor Busbee mentioned, of the so-called entitlement programs in which you are involved—that is AFDC and medicaid.

I am curious to know what gives anyone the notion to suggest in the sorting-out process that, somehow or another, welfare programs or basic income security programs are a Federal responsibility. In the genesis of the federal system it was a private responsibility, then it was a community responsibility, and then it was basically a local and State government responsibility. Now the whole load seems to be dumped on to the U.S. Congress, at least by a number of people at the State and local level who say it is somehow our responsibility to take care of these programs.

You have just demonstrated the degree of the lack of confidence in Congress' ability to address this in an appropriate way.

Let me ask you to discuss medicaid and AFDC and an appropriate role of discharging these responsibilities.

Mr. SNELLING. Thank you. Senator, the Governors have been for quite some time as united on that subject as we have been on anything. Our feeling really is that you have to see what has happened since the Constitution was written, and since those early assumptions that charity was a local and a private matter, to understand our concern about that notion.

Clearly, for example, immigration policy dramatically affects the burdens that a particular State or community is going to feel with respect to its obligations to the poor. How could we have an open door policy, for example, and then hold Florida totally responsible for the welfare function after its experiences as a result of national policy with massive immigration? Clearly, that national economic policy determines the viability or the level of employment or unemployment in Detroit. It isn't strictly a matter for the voters of Michigan to determine, nor do they have the capacity to control the level of employment or unemployment.

So 200 years of Supreme Court and congressional implementation of the "common welfare" clause of the Constitution has made a far

more homogeneous Nation than once existed. We no longer have a bunch of little hamlets where the people really can accept the responsibility for the welfare of their own.

The Governors' position has not been at all inflexible on this. What we have said is that the common welfare clause of the Constitution gives the Federal Government the responsibility to set some minimum levels or safety nets, if you will. The Federal Government must do that in terms of national philosophy and goals. In order to have it work in a time when transportation makes it so easy for people to flow from one region of the country to another, the setting of minimum levels or safety nets ought to be a responsibility of the Federal Government.

Governor Busbee has done a great deal of work on this. It isn't as though we say that without a willingness to do the sorting out to which you have referred. We don't understand how education or transportation—except for interstate—or law enforcement, got to be the responsibility of the Federal Government under the Constitution, but that is the historic justification.

Senator DURENBERGER. Any other reactions from the other Governors?

Mr. BUSBEE. Senator, I would join Governor Snelling and say this is nothing sacred to us. If we could get into a true sorting out process and remove all of this duplication and determine who could best administer which programs, I think we would be wide open to specific suggestions.

Now the problem is, though, when you come to the income maintenance programs, you have had a long history of involvement at the Federal level. We have felt that if you are going to have social security and all of the income maintenance programs, then logically you should have medicaid and welfare, rather than splitting the basic responsibility for income maintenance.

I am not inflexible in talking to you about any sorting out proposal, if we can do it over a period of time. But I do think it makes much more sense if you had the income maintenance and we had the domestic programs which you are so deeply involved in now—like education, transportation, law enforcement, community development, and many, many other programs. We are not looking to gain anything in money from the swapping process. The question is who can do the job best.

I just really think it is wrong for the State governments and the Federal Government to be involved in everything and try to be all things to all people. Take education. You put up 7 percent of the money for education. We put up the balance. It is not a question of whether we can absorb this 7 percent—which would be a legitimate item to talk about—but you leverage 52 percent of the education budget when you put up 7 percent of the money.

People's needs are totally different in Alaska from what they are in metro Atlanta. When you take some of your Federal programs, they not only control the limited Federal money made available, but they sometimes screw up the balance of the program for us, too.

We are not in concrete on any of these items. We would be glad to start out from the beginning and not with a preconceived plan.

Mr. MATHESON. I certainly agree with Governors Snelling and Busbee. Philosophically, according to the last meeting we held with all of the Governors, they are anxious to come forward and sit down

with the policymakers here in Washington to fairly and equitably distribute the burdens and the costs of public service. I see that interest growing on a very profound basis.

One reason why the income entitlement programs seem to fit at the Federal level better than at the State level is because we have very little capability to control the management of those programs. If we could manage and control it better—but, for example, with immigration back and forth across the Atlantic being 20 percent of the people a year or nearly that, it gives us a situation which is not under our management capability. Philosophically I think we should sort out which level of government can perform the best. All of the information which is valid to that decision should be the basis to do it.

I believe if that process became real, we could find answers on either side. As has been said, we are open to that kind of open discussion.

Senator DURENBERGER. Senator Danforth?

Senator DANFORTH. That is, I think, the irony. The coincidence is that I just came here from a hearing in the Commerce Committee on the proposal for a national bottle deposit bill. Vermont, I know, has one. Maybe it is just a great idea at the State level. But my point at the hearing, and I seemed to be alone in stating this, was that there has to be something that the Federal Government doesn't do. Whether you agree with the program or not, whether it is a good program or not, there has to be something where we say just as a matter of decision-making responsibility we don't do that kind of thing.

In any event, I wanted to ask you about predictability. This is a point that Governor Snelling especially stressed. It is a matter that is of some discussion in Washington, because we clearly have a problem with the budget. Everybody has been talking about it today. The figures change weekly, if not daily. We are given this moving and growing target to shoot at. We are going to have to do something about it, a lot of things about it.

One of the old sayings is that, "Well, we can't do anything on the revenue side because we have just passed a tax bill. My gosh, if we were to redo that, nobody would have confidence in what we are doing and there wouldn't be any predictability."

I take it that your testimony is that, as far as State government is concerned, the greatest threat to predictability is in appropriations, not in what we do with respect to the other two areas, which are revenues and entitlements. You have gone through the process of cutting back on appropriated items last spring and summer. Then the second shoe—what is it, 12-percent additional cuts—falls on the proposed appropriated amounts. By the way, there are many billions of dollars of unspecified cuts that we are going to have to come up with later. This constant hitting you with phase 1, then phase 2, then phase 3, and how many more phases of appropriations—the result is that among the three possibilities, current budget instability is absolutely the worst with respect to predictability. Is that correct?

Mr. SNELLING. Yes.

Senator DANFORTH. In fact, we have kept you so off balance that it is very difficult to proceed in an orderly fashion in State government today. Is that right?

Mr. MATHESON. That is absolutely the case. At the last moment, Senator, we put together the budget having absolutely no way to predict what the cuts or the amounts will be. There is uncertainty.

Senator DANFORTH. Would this be true of local governments as well? Or, is this something that is just pretty much a problem of State governments?

Mr. SNELLING. It is true of both State and local governments. I think you will find the most frequent questions asked of Governors or mayors by the public or the press is, "How much are you going to have to raise your taxes in order to provide a decent, reasonable level of government given the Federal cuts?"

This is responsive to your first question. It isn't as though the public has the impression that on the revenue side the matter has been finally adjudicated and can go forward. The public has no confidence that that is true at all. What they believe is State and local governments are either going to have to make some horrible choices regarding service cuts, or they are going to get it by raising revenues. Franklin Roosevelt, in a dramatic moment said, "We have nothing to fear but fear itself."

I submit the kind of concern that is now growing out in the countryside about the ability of the budget and the stability of taxes is causing a great fear. Exactly as you said, we have had the cuts. We haven't even accommodated them. The fiscal year has started. What we are constantly being told, the phrase which was uttered in this room a half a dozen times already, what we are constantly being told is:

You haven't seen anything yet. Now, Governors, go back and calm your people. Tell them this is a rational government and we are going to provide safety nets. But you haven't seen anything yet.

Senator DANFORTH. Then predictability, when we talk about lack of predictability, is flowing from not just one effort at appropriations, but one followed by another with another one foreshadowed.

As I understand it, what you are saying is that these budget changes are not just a burden on the planning capabilities of people in Montpelier or in Jefferson City.

Mr. SNELLING. No.

Senator DANFORTH. But instead it is a lack of certainty on the economic future of the communities, of individuals. Am I right on that?

Mr. SNELLING. Right. And also the special interest groups. If you were sitting down with a special interest group in your State and talking about taking care of people and you say, "Here is the extent of damages and hereafter we are going to have to accommodate inflation." That would be one thing. But basically we can't lie to them. We have to tell them what we know. We have to say, "This year this is what we think we will have to do." They say, "What about next year?" We say, "We can't even tell you. This deal we are trying to negotiate with you for today depends on what the Congress will do with respect to the 1982 budget."

So I think we are exciting all of the special interest groups and virtually everyone at every level because of a lack of stability at precisely the time we need it.

Senator DANFORTH. Is it just the special interest groups who are the beneficiaries of various State programs; or do Federal budgetary

changes have an impact on the private sector as well, on the business community? Does it have any impact there?

Mr. SNELLING. Oh, I think so. Certainly I think it does. Absolutely.

Senator DANFORTH. People involved in highway construction and bridge building and so on and so forth?

Mr. SNELLING. Certainly.

Senator DANFORTH. Does it have an effect there?

Mr. SNELLING. Yes, I think it does.

Senator DANFORTH. If we were looking for a program which would close the deficit—and I think almost all of us want to do that—and do it in a way which is reasonably predictable and causes less confusion and uncertainty throughout the country, how would you suggest we go about doing that? What would you advise us to do?

Mr. SNELLING. That is an individual answer. I can give you mine. Governor Busbee will give you his and Governor Matheson will give you his.

Senator DANFORTH. It would not be hitting appropriations.

Mr. SNELLING. Pardon?

Senator DANFORTH. I am just talking about the big areas—the appropriations, the revenues and the entitlements. You would essentially lay off the appropriations, correct?

Mr. SNELLING. I would stabilize them and give some sense of forward levels. I would say that if we were to stabilize appropriations wherever they could be stabilized—you can't with respect to all; there are some true uncontrollables and there are some political difficulties—then appropriations no longer could rise at the rate of inflation. On the revenue side I would argue it really isn't any sin to agree you have done the right thing at an excessive rate. In business if you put through some price increases and they don't fly, you don't get fired by the board of directors if you roll them back to the level at which they do fly. You could get fired, however, if you don't roll them back to the level at which they will fly.

Senator DANFORTH. As I understand it, what we have done so far since last January 20 is to say, "We think that the country has been heading in the wrong direction. We are going to try to control the rate of growth in Government. We are going to try to provide the kind of tax program which encourages the expansion of the rest of the country." Setting out on that direction and sticking with it does not necessarily entail locking in permanently on each detail and each step along the way, does it?

Mr. SNELLING. You are absolutely right. I wish that what you just said would be the philosophy guiding the administration and the Congress of the United States right this moment.

Senator NUNN. I could say I agree with that.

Senator DANFORTH. You three are politicians. Would the country rise up in arms if we decided that, instead of the tax cut taking place over 3 years, it were to take place over 5 years, thereby saving $41 billion in 1984 alone?

Mr. SNELLING. If you told your wife you were going to give her a beautiful present on Thanksgiving and later you told her it would be Christmas before you delivered it, would she be terribly, terribly upset?

Senator DURENBERGER. Unless you have been promising it for a long time and she has reason to doubt that Christmas is coming. [Laughter.]

Senator Nunn?

Senator NUNN. I would just like to agree with the Governor's statement that making a change doesn't mean you weren't heading in the right direction. I completely endorse that. I think it is beyond belief to me that people can become so locked in and so rigid philosophically that they cannot look reality in the eye. The reality is that there will be no way to get the budget under control unless there is a combination package of both revenue and expenditure cuts.

Yet, as I mentioned a few minutes ago, Senator Domenici is trying to put such a thing together. At every step he gets rebuffed. It is because some people are so rigid that they don't want to say they could have gone a little too far in the right direction. So I completely agree with that.

Let me just ask a question of the Governors. What are your projections for fiscal year 1982 in terms of your own revenue growth? In other words, what kind of economic forecasts are you using as assumptions? The Federal Government is using 5.2-percent real growth rate, which is about to be radically and dramatically cut back. What kind of growth rate are you using in the real growth of your budget?

Mr. SNELLING. We are using 1.9 in my State with all of it coming at the end of the year.

Senator NUNN. But that would be—your fiscal year starts in July?

Mr. SNELLING. July.

Senator NUNN. Governor Busbee, what are you using in Georgia?

Mr. BUSBEE. When you say real growth rate, now——

Senator NUNN. Above inflation.

Mr. BUSBEE. These are fictitious figures we are using because I have approximately 4 percent built into my budget for inflation in the State government, but on the revenues it would be 9 percent.

Senator NUNN. Nine percent growth in revenues?

Mr. BUSBEE. That is right.

Senator NUNN. There would be almost no growth, though, above the rate of inflation—this rate of inflation?

Mr. BUSBEE. That is right.

Senator NUNN. So you have almost a zero percent or 1 percent growth.

Mr. BUSBEE. It would be in real terms, yes.

Senator NUNN. Governor Matheson?

Mr. MATHESON. Our growth rate revenue rise has been below inflation for the last 3 years. The second year that I was Governor we created 35,000 new jobs in our State. For a State the size of Utah that is an incredible performance. The past fiscal year we created 1,500 new jobs in the State of Utah, to give you an idea of how flat the economy is in that area. From reading the analyses of fiscal problems in all of the States, I don't think that any Governor, with maybe one or two exceptions, could give you a very positive report about that.

Senator NUNN. You see, in Congress right now in the Budget Committees and Appropriations Committees, they are in the process of making all sorts of decisions. Yet all of the budgetary figures are still based on a 5.2-percent real growth rate. One of the President's top economic advisers, Dr. Jerry Jordan, testified 6 or 7 weeks ago before

the Small Business Committee that this was unrealistic. So people are about to throw up their hands in futility here because things have changed so rapidly. They are not going to make a new forecast until December.

We are faced, to some degree, with the same thing you are. Senator Mattingly has been making moves to cut some appropriations on the floor. Most people will be voting against it because most people are saying, "What is the use? We cut $2 billion here and another $2 billion there. Then the next day somebody is going to come around, say December 1, and say oops, we were wrong on the growth rate. It was 2 percent. We are now in deficit about $30 billion more."

That is just around the corner. In December, we are going to see a revised growth rate that completely eliminates all of the assumptions we have been working on. The deficit, no matter how many cuts we make between now and December, is going to go up. That is the incredible lack of certainty that we are dealing with.

Let me ask one other question. Governor Busbee, what does the State of Georgia do about indexing taxes? Do we have indexing of taxes; that is, holding taxes steady even with inflation?

Mr. BUSBEE. No.

Senator NUNN. Do you advocate that at the State level?

Mr. BUSBEE. We reduced taxes slightly last year. We will have no tax increase at all. The only thing we are faced with now, as far as taxes, is how much they will be reduced because of what you did here in the Congress. We are not going to be able to make the reduction we ordinarily make.

Senator NUNN. Governor Snelling, do you index taxes?

Mr. SNELLING. In all fairness, we ought to point out the differences that our various States have, for openers about the level of tax burdens. My State is the ninth most heavily taxed in the 50 States in terms of percentage of per capita income that we derive. We are not able to index. We have been reducing tax rates over a period of time minutely in the field of income tax and the others, but we do not have any formal program of indexing.

Senator NUNN. Governor Matheson.

Mr. MATHESON. We do not index in Utah. We have kind of a special problem out there. We have the highest birth rate of any State in the United States. In fact, I think we are the grand champions 7 years in a row, and going for an eighth. To give you an idea of the problem we have in educating our youngsters, our income tax all goes into the uniform school fund. We simply couldn't afford to index and educate those kids. So, I am hoping no one will throw a bill in the hamper to try and change it. We simply couldn't survive.

Senator NUNN. Two other questions, Mr. Chairman, and I will yield.

Do you believe, Governor Snelling, that the tax cuts which have been enacted have gone too far?

Mr. SNELLING. Yes, sir, I do.

Senator NUNN. And you are saying, this morning, that we need to take another look at those.

Mr. SNELLING. Yes, sir.

Senator NUNN. Governor Busbee.

Mr. BUSBEE. I agree.

Senator NUNN. Governor Matheson.

Mr. MATHESON. Absolutely. I think that Senator Domenici is absolutely on the right track. People are willing to take pain as long as they can see it is the right thing to do. I think the public is ready for that.

Senator NUNN. Thank you, Mr. Chairman.

Senator DURENBERGER. I want to get to the whole resource turnback issue before we finish. We only have a few minutes left. On the other side of the question I asked earlier concerning medicaid and AFDC—which got us a bit into the so-called sorting out notion—is a problem that is present for cities in this country, in particular about some of the things we are doing. It seems to me that, if you look inside that $85 billion pipeline, you will find a great big reaction to the fact that over the last 25 years or so the States have failed city governments in this country. We decided instead that we, the Congress, would impose a tax on the suburbs and run it via categorical grant programs to the cities to keep them alive.

It seems to me that, if my inclination is to go along with your recommendation, we should return more of the so-called place-oriented programs to State governments—in particular, transportation, community development, sewage treatment, the infrastructure issues. What is there out there to prove that the States now are prepared to address the problems which sent local governments to Washington in the first place? What is the States' record in meeting those kinds of needs which you ask local governments to deliver in your State?

Mr. SNELLING. Senator, you know that ACIR has documented a tremendous increase in the capacity of the States to deal with these kinds of problems. There are State-by-State examples of the effectiveness of the State ACIR-type commissions and the whole process which has grown up over recent years for dealing with local problems. Probably at bedrock, however, we may have to face the fact that the Federal Government was created by the States who had the authority as sovereign States to do so. The relationship between communities in each of these entities—there is a great difference from State to State in those relationships.

I would argue that the States need to adjudicate and compromise with the Federal Government the proper relationship, given the constitutional background. There is clearly just as much duty and responsibility for the States to do right by the people in their States, whether they are urban people or rural people. That is happening, we believe, in the political process.

The National Governors' Association, as you know, has taken a great number of initiatives in this area. We now have a new committee, a full standing committee, whose only task is to bring ourselves more into accord and to create a new liaison with the towns and counties and sub-State governments.

Senator DURENBERGER. Senator Mattingly, do you have any questions?

Mr. MATHESON. May I make one comment? Pardon me, Senator.

It has been my judgment that in the last dozen years, or maybe 15 years, State legislatures have been less than willing to delegate to local units of government the capability to operate successfully.

In my State, for example, a city and a county lives or dies on property taxes and local option sales taxes and fees. They are just

absolutely held down economically. If we are not willing, at the State level, to delegate the necessary tools for them to do their jobs, then we are not going to succeed. There is a legislative hangup to delegate just like there is a legislative hangup here with some people in the Congress—not all, of course—to put the block grants in the States. We are preaching to the choir today, as Senator Domenici indicated.

I think the Governors have a real responsibility in the budgeting process to design public policies so that the sorting out process works. They can do this by delegating to the local units of government that piece of government which it does the best, and by manipulating and managing the dollars so that we can push down those services at that level in the same philosophical sense that we talked about between the Federal and State governments. In fact, my whole budget process this year was guided by that approach. I sorted back to the local communities—with funding, incidentally—those very things which I think, in the long run, will reverse the trend which you have described with which I agree.

Mr. SNELLING. Can I give you two quick statistics to prove this. Fifteen years ago local governments financed 55 percent of the cost of State and local services and the States financed 45 percent. Today these proportions are reversed with States carrying 57 percent of the load. Furthermore, during the same period of time, when direct grants from the Federal Government to local governments rose from $2.2 billion—which was in 1965—to $19 billion in 1978, States' support of local functions grew from $20 billion. In other words, it started in 1965 at 10 times the then Federal level and was more than the Federal level had reached and has grown to $86.6 billion in 1978, an increase of 319 percent.

When Governors tell you about the burdens on their States, a very large part of what they are talking about is the burden of meeting their responsibilities to the community.

Senator DURENBURGER. Senator Mattingly.

Senator MATTINGLY. I have listened to all my colleagues here criticize the tax cut, basically. Let me just try to put something in perspective for you, though, since I happen to be on the other side of that issue. I feel that the economic recovery package is in place, or part of it. Part of the economic recovery package was the tax incentive programs. There is no doubt, and I can look at our State of Georgia—outside of the aggressive pursuit of yourself, which has been outstanding for the last 7 years, of getting industry into our State—but there is no doubt that the incentives which were given by our State and the lower tax structure in our State, comparatively speaking to the city of New York, are things that entice industry to come to our State. Wouldn't you agree?

Mr. BUSBEE. I would think so.

Senator MATTINGLY. And this new economic package—even though you all may think it is excessive, there is also the chance, probably a greater chance, that it will succeed in restoring incentives back into the private sector when they all go into effect.

I think what we are all trying to do is create an atmosphere, a positive atmosphere, where we can get the growth rate in our country to go up.

In order for us to get a handle on the budget, you have touched on one item today, which I think is to me tremendously important, which is the entitlements. We have to control entitlements and change that process. We need your backing.

There are other areas in which there will be some additional cuts in controllables; however, I think these cuts will be minimal. There also has to be an approach to get the waste, and none of you mentioned this, or any abuse out of the Defense Establishment. That has to be done. This is a tremendous amount of money.

Now, given those three budget areas in which we have plenty of areas to work which this tax package covers, I don't think now is the time for us or anybody else to panic over the tax program. I think it is a time to allow it to work, though. Give it an opportunity to go to work and then see if, via the tax incentives, we can't get the country to grow. We have gone through a couple of heavy decades with high tax rates. Let's try and see if we can't make this country grow via incentives, not disincentives.

Senator DURENBURGER. Governors, we have only a few minutes left. I will capsulize my question on the resource turnback issue and ask you to respond either from the association's perspective or an individual perspective.

Our options on equipping you to pick up these responsibilities are several. First, the administration's option, the so-called taxroom theory—it is that the tax bill, which has been criticized much here today, has created some room for State governments to move in with increased taxes or new taxes and take up the gap. The problem with that is it also runs against the supply-side economic theory, if you buy that theory. I would like you to speak to the taxroom theory.

Related to that, I would like you to speak to the impact of the tax cut, particularly the corporate depreciation. Some States piggyback on the corporate tax. What do you see by way of State reaction to the implications on State revenues?

What is your reaction to general revenue sharing as a form of working our way out of the pipeline? What is your reaction to the proposal, which some have made, that the Federal Government increase excise taxes on "sin" rather than leaving it to those who know more about "sin" at the State and local level? Would you comment on Senator Domenici's megablock theory, which brings us back to the use of block grants again as a way of resource return?

What are your thoughts about the proposal I made last week? It would permit the States a surcharge or a surtax on the Federal individual income tax at the election of the States, and only after they have either made an election or we have evolved to the States full responsibility for the list—perhaps similar to some of the lists which Pete forwarded here, of current category called block or entitlement programs.

Mr. SNELLING. Very quickly, we all continue to think that revenue sharing is perhaps the purest form of block grant that there is. If there is any reason for the Federal Government to collect taxes in the first place, it must be because there is some national purpose either in the collection or distribution of the funds. So turnbacks, if they were simply to be a turnback exactly in the same proportion which

they were extracted in the States, would seem to be, in effect, a non-Federal function. If turnbacks make some effort to achieve some national policy of equalizing opportunity or the like, that could make a great deal of sense.

With respect to the megablock proposal, I for one think it has a great deal of merit. Individual States may very well be attracted by this concept. The proposal, even in its definition, however, does not offer any solution to the problems that your subcommittee is facing. What it deals with is a period down the line where 5 States out of 10, or something like that, have a chance to demonstrate.

Senator DURENBERGER. Is anybody doing anything with the House-conceived notion of kicking back categoricals in exchange for the State's share of general revenue sharing?

Mr. SNELLING. I think that has been very significantly considered. At the moment, however, the items that we discussed earlier are higher on our agenda. I think your boilerplate proposals are very, very important. I think we could find a better name for them. The notion that congressional legislation ought to always be drafted with an eye to the extent that categorical programs could be lumped together and States given some latitude, is very important in bridging this immediate period.

Senator DURENBERGER. Any other comments?

Mr. BUSBEE. I think your time is about over, but I would like to express my appreciation to you and to the members of your subcommittee for hearing us today. I hope this won't be the end of this conversation.

Senator MATTINGLY. One last comment.

Would you all try to respond, if the excise tax proposal comes to pass, about what formula you might have for exchanging revenues and expenditures with the Federal Government? Tell us whether you want to share that or how you would propose doing that. Also, when would you have that?

Mr. SNELLING. We can discuss that with the leadership and see if we could find answers for you as soon as possible.

Senator DANFORTH. I just want to say, Mr. Chairman and Governors, that this really was one of the best hearings I have attended. It has been very helpful. I would hope that there would be some regular process—maybe, I don't know, in this subcommittee or some other process—of having this kind of exchange on a continuing basis, on a regular basis.

The issues that were discussed are obviously fundamental. Oftentimes around here we get into specific bills, details, and we lose sight of the big question. Well, this has been a morning of discussion about very big questions. I would hope that some systematic means would be found, Mr. Chairman, to continue this dialog on a regular basis.

Senator DURENBURGER. Thank you for summing up the feelings of all of us who have participated in the hearing today. I thank you, Governor Snelling, for suggesting this occasion to us. We will count on all of you to continue the dialog in one form or another.

Mr. SNELLING. Thank you very much, Mr. Chairman.

[The prepared statements of Governors Snelling, Busbee, and Matheson follow:]

PREPARED STATEMENT OF GOVERNOR SNELLING

Mr. Chairman and Members of the Subcommittee, if there is an underlying theme to the testimony you will hear today from three governors from diverse states and different political parties, it is the need to dispel the clouds of uncertainty that overhang the federal system and that are hindering the ability of state and local governments to respond to the challenge of President Reagan's federalism initiatives.

This uncertainty has several elements. As most State governments enter the fifth month of their 1982 fiscal years, they do not know the final level of funding of many Federal programs they administer. As governors across the country begin in the next few weeks to complete their fiscal 1983 budget recommendations for presentation to the legislatures in January, they do not know where tens of billions of dollars in unidentified 1983 and 1984 budget cuts will fall. As state and local and even business leaders contemplate shrinking federal aid and unprecedented interest rates for tax exempt borrowing, they are concerned that public infrastructure needs crucial to economic growth, such as highway and water systems, will go unmet. And as state and local officials everywhere contemplate the deep funding cuts and limited flexibility in the current block grants, they ponder how far the block grant approach to federal funding is worth pursuing.

We are here today not just to outline these problems but, as the past, present, and future chairmen of the National Governors' Association, to recommend a plan for attacking them that we believe will meet your concerns as well as ours.

On September 24, the day that President Reagan presented his request for additional funding cuts to the nation, our Executive Committee met and unanimously adopted a six-point statement that summarizes our concerns. We discussed these six points with the President that same afternoon, and we have communicated them to the leaders and Members of Congress in the intervening weeks. I would like to submit them now for the record.

Our testimony will amplify these points. Each of us here today is prepared to report to you how we are implementing the block grants enacted by Congress last summer and to discuss with you the omnibus block grant requirements on which your subcommittee has been working and which we believe are essential if further progress is to be made in simplifying the Federal system.

I would like to focus the remainder of my remarks on the importance of fiscal stability to the success of the President's program and to suggest how it can be achieved. By fiscal stability, I mean early agreement on an overall funding level for aid to State and local governments. Governor George Busbee of Georgia, our immediate past chairman, will focus on how the management problems confronting State and local governments could be further reduced by agreement on a gradual but steady sorting out of Federal, State and local responsibilities. Governor Scott Matheson of Utah, who will succeed me as chairman, will discuss the need for greater certainty in public infrastructure programs such as water and highways and will briefly discuss revenue turnbacks in this context.

Mr. Chairman, as I am sure you already know, it is possible to conceive a scenario under which virtually all Federal aid to State and local governments disappears by 1984. Indeed, Alice Rivlin, Director of the Congressional Budget Office, presented a scenario to the Congress in September that suggested that there will be only $8 billion available in 1984 to fund more than $40 billion in discretionary grants to State and local governments. Clearly, that would be an unacceptable result not only to the nation's governors and mayors but to its Senators and Congressmen and more importantly to the people.

Nevertheless, it shows the enormous pressure that the so-called "uncontrollable" Federal expenditures are exerting on Federal aid to State and local governments, which makes up most of what is left in the budget once defense, entitlements, and interest payments are excluded.

The pattern of Federal budget cuts thus far, beginning in the last 3 years of the Carter administration and continuing in the Omnibus Reconciliation Act and the Reagan administration's latest request for a second round of cuts, suggests that the uncontrollable programs will continue to be just that. In the reconciliation bill, for example, State and local aid, which makes up about 15 percent of the Federal budget, absorbed about 33 percent of the cuts.

Obviously, State and local governments have adequate grounds to express concern about the level of future funding and to press our Federal partners for greater consultation in 1982 and 1983 budget decisions, which we hope will be made very soon.

Insofar as I have been able to determine, the administration has published just one long-range forecast of State and local aid. That forecast is tucked away on page 124 of the administration's March 10 budget proposal. I would like to suggest that it become the basis for an agreement on stabilizing the federal system while further adjustments are worked out. Accordingly, I have attached to my testimony a copy of that forecast.

You will note that this forecast divides state and local governments into two categories: first, payments for individuals through state and local governments, which I will refer to as federal-state entitlement programs; and second, all other grants, which I will refer to as discretionary programs.

The administration is forecasting growth of about 4 percent a year in the federal-state entitlement programs and virtually no growth in the discretionary programs. Overlying this forecast of last March, however, was the uncertainty of unidentified federal aid cuts totalling about $75 billion in 1983 and 1984. Today, that uncertainty has grown to more than $100 billion.

There are four possible approaches to deal with this uncertainty:

Increase federal taxes; slow down the defense build-up; control the growth in entitlement programs; and continue to cut state and local discretionary grants.

Although governors individually have their own views about the proper level of federal taxation and defense spending, we do not regard it as our role to make specific recommendations through the National Governors' Association on what are essentially federal responsibilities. Obviously, we would be concerned if the federal government attempted to pre-empt what have been traditional state and local revenue sources, such as sales or excise levies, without consultation. Such a move would totally contradict President Reagan's promise to return revenue sources to the states. In addition, our Executive Committee unanimously expressed the view that all portions of the federal budget, including defense, be scrutinized for potential savings.

Entitlement programs and the federal aid system are the other sources of potential savings. As we discuss the intergovernmental grant system, we should keep in mind that this sector of the budget addresses the nation's most important domestic goals. For these programs I would like to suggest an approach that is consistent with the principles we adopted on September 24 but whose specific funding recommendations go beyond what the National Governors' Association has yet addressed.

I propose that we agree on the administration's long-range forecast of level funding at about $46 billion a year for discretionary grants to state and local governments for 1983 and 1984. We would thus be foregoing normal economic growth in these programs. This would mean that real levels of aid would decline at the rate that the purchasing power of these federal dollars is cut by inflation. It would mean that the uncertainty of unspecified additional funding cuts would be lifted from these programs. It would enhance the ability of both federal and state and local officials to plan for meeting our joint domestic responsibilities.

From the viewpoint of the governors, it would also accomplish two other important goals. First, it would set the stage for further simplification of the federal aid system under fair ground rules. If inflation cuts these grants by 10 percent or less, then some of the savings could be accommodated by consolidation of the nearly 500 remaining categorical grants and by further streamlining of federal regulations.

In that context, enactment of the "boilerplate" block grant language that this subcommittee is working on would be extremely important. I want to reiterate the support for this important effort that was expressed by Stephen Farber, our executive director, in his recent testimony before you. We also strongly support Senate Bill 807, the only comprehensive grant reform bill pending before Congress, which would streamline congressional consideration of grant consolidation programs and reform intergovernmental audit procedures.

Second, stable funding of these programs over the next two years would preserve the option of a sorting out of federal, state, and local government responsibilities along lines that we and the Advisory Commission on Intergovernmental Relations have recommended, with a stronger federal role in income security programs in exchange for a stronger state and local role in education, transportation and other areas. Unless we preserve these programs, the sorting out option will be foreclosed.

The entitlement programs should be exempt from the level funding ceiling but not from budget scrutiny. Although federal-state entitlements such as welfare and medicaid represent far smaller portions of the federal budget than the

direct federal entitlements such as federal pensions, social security and medicare, the entitlements we administer have absorbed a disproportionate share of the cuts thus far. The administration's March 10 forecast shows this disparity continuing, with direct federal entitlements projected to grow at more than twice the rate of federal-state entitlements through 1986.

There are clear relationships between many of the entitlement programs run by the Federal government and those run by the states—between medicare and medicaid, for example, or between food stamps, welfare and unemployment compensation. Although the problems of the direct federal entitlements must ultimately be addressed by federal policymakers, governors are willing to work with the Congress and the administration in addressing the entitlements issue, if we can be assured that the programs we help fund and administer will be treated fairly. Such an effort should explore not only the potential for savings but the question of what are the basic standards of need that we as a nation want to meet and how should the burden of meeting those needs be apportioned.

Together, direct federal and federal-state entitlements total about $340 billion in fiscal 1982 and will total almost $400 billion in 1984, or about 45 percent of the entire budget. Given the size of these programs, their overlapping nature and administrative complexity, the questionable wisdom of the manner in which many of them are indexed, and the undeniable need for a more effective way of coping with spiraling medical costs, it should be possible to achieve savings without inflicting undue hardships on those who depend on them for their basic needs.

Frankly, governors are not encouraged by the way that entitlement programs have been addressed thus far. The safety net has been made more secure for beneficiaries of direct federal entitlements, where eligibility often does not depend on need, than for beneficiaries of federal-state entitlements, where need is always a factor. Efforts to address direct federal programs have been undermined by premature proposals and political responses, and the result is that the one-third of the federal budget represented by direct federal entitlements—a portion that exceeds even the defense budget—has largely escaped scrutiny.

In summary, the governors want to continue to work with the Congress and the administration to control federal spending and to strengthen our federal system. We are prepared to shoulder increased responsibilities as long as the ground rules for change are clear and fair and the pace of change is reasonable. We have shown our good faith by moving quickly to implement the new block grants, despite the steep funding cuts, lack of lead time, and limited flexibility that accompanied them. We now ask our federal partners to show their good faith by negotiating further changes in the federal system in a manner that recognizes our concerns. In so doing, we can together insure that the renewed spirit of federalism that is abroad in our land will endure.

TABLE 18.—COMPOSITION OF BUDGET OUTLAYS, 1980–86

[Dollar amounts in billions]

	Actual,	Revised budget estimates					
	1980	1981	1982	1983	1984	1985	1986
National defense:							
Direct Federal payments for individuals	$12.9	$13.8	$15.3	$17.1	$18.7	$20.2	$21.6
Grants to States and localities	.1	.1	.1	.1	.1	.1	.1
Other	123.8	148.3	173.4	208.9	235.9	283.7	321.1
Subtotal, national defense	135.9	162.1	188.8	226.0	255.6	303.9	342.7
Nondefense:							
Direct Federal payments for individuals	237.0	278.0	298.2	323.8	348.3	374.6	393.4
Payments for individuals through States and localities	34.2	39.4	39.1	41.5	43.5	45.5	47.3
All other grants to States and localities	57.2	54.9	47.2	45.7	44.3	44.2	45.1
Net interest	52.5	64.1	68.2	68.9	67.8	64.9	62.8
Other	63.0	56.6	53.7	55.8	54.9	51.8	58.4
Subtotal, Nondefense	413.8	493.1	506.5	535.7	558.9	533.9	612.0
Total, Revised budget	579.6	655.2	695.3	761.8	814.1	837.7	954.7
Additional savings to be proposed				−29.8	−14.2	−13.7	42.7
Target outlay ceiling	579.6	655.2	695.3	732.0	771.2	844.0	912.0

Source: Fiscal 1982 Budget Revisions, Executive Office of the President, Office of Management and Budget, Mar. 10, 1981.

Attachment.

NATIONAL GOVERNORS' ASSOCIATION,
September 24, 1981.

KEY ISSUES OF CONCERN TO THE GOVERNORS

During the past six months the Governors have generally supported efforts by the Administration and Congress to control federal spending despite problems for state governments caused by the budget cuts, the short lead time for their implementation, and less than adequate flexibility provisions. With regard to further budget and revenue proposals now under consideration, we believe that the following points are important:

1. Further spending reductions must be fairly apportioned throughout the budget, including defense. Further cuts in domestic spending must move the federal system toward a clearer and more rational division of responsibilities among the Federal, State, and local governments. We will judge each proposal on whether it reinforces the federal role in income security programs, which are a national responsibility, and the state and local role in such areas as education, law enforcement, and transportation.

2. In particular, we will continue to oppose vigorously any attempt to shift a greater portion of the Medicaid burden to the states. We will work with the Administration and the Congress, however, in efforts to hold down the costs of Medicaid and Medicare through measures designed to promote competition and reward efficiency and other means.

3. We will oppose any attempt to make deeper cuts in fiscal 1982 or 1983 in the new block grants. These programs, which will account for less than $7 billion of the $88 billion in federal grants administered by state and local governments, have already absorbed reductions ranging from 20 to 25 percent. No further cuts should be made until states have had an opportunity to adapt to the substantial changes that have already been made.

4. We believe that plans to phase out federal responsibility for the wastewater treatment construction grants program should provide for an adequate transition period to develop alternative funding sources. They should also contain greater flexibility for states to direct funds to priority water quality and public health problems than is contained in current Administration reform proposals. The fiscal year 1982 budget should include $2.4 billion for the program, as the President proposed in March provided workable reforms are adopted by Congress.

5. We will work with the Administration to develop workable proposals for a meaningful turnback of federal revenue sources to the states, despite such difficult problems as state-by-state distribution effects, in highway finance and other areas. The only current turnback program, revenue sharing, should be preserved.

6. The Administration should establish an "early warning" mechanism to ensure that the states are fully consulted not only on federal budget cuts but also on the development of any policies that touch on federal preemption of state powers and responsibilities. Recent examples of such issues include the abrupt ruling of the Internal Revenue Service to deny tax exempt status to certain small-issue industrial development bonds—a ruling which should be withdrawn immediately—and Treasury Secretary Regan's call last week for an overhaul of federal laws governing the regulation of banks and other financial institutions.

[Adopted at Executive Committee meeting, September 24, 1981.]

PREPARED STATEMENT OF GOVERNOR BUSBEE

Mr. Chairman, I'd like to outline briefly for this subcommittee the problems the States are encountering in providing effective and responsible fiscal management in a time of tremendous uncertainty in Federal-State relations.

Although nearly two-thirds of the budget cuts included in the Omnibus Reconciliation Act were in grants-in-aid to States and localities . . . and although the Federal tax cut package immediately created a loss of revenue for many State governments whose income tax laws tied directly or indirectly to the Federal income tax laws . . . it is not my purpose in appearing before you to complain about the magnitude of these budget cuts and revenue reductions to States.

What I am here to describe to you is the overriding problem the States have had with the Federal budget process.

As this administration entered office facing a chronically troubled economy . . . and an ever-increasing sense of public disillusionment with government in general, the Governors, in a bipartisan way, supported the President and the Congress in their efforts to make a fundamental change in the very nature of American Government.

We recognized that it was imperative that the Federal budget be brought under control and we knew that this would necessitate programmatic changes.

Despite the fact that nearly two-thirds of the budget cuts included in the Omnibus Reconciliation Act were in grants-in-aid to States and localities and were administered by States through their budgets, there was no prior consultation by the administration with most Members of Congress nor by either the administration or Congress with the States that were affected. As a result, we not only have a Federal budget that is not balanced, but the budgets of the States are in disarray and chaos.

As you know, many States are mandated by their constitutions to have a balanced budget. Prior to this action by the administration and Congress, the budget process in State governments consisted of an orderly flow of actions beginning with preliminary revenue forecasts and identification of continuing needs of State government. The Governor received agency funding requests, met with his budget analysts and agency heads and developed a budget recommendation for the legislature, including whatever improvements revenues would permit. The legislature then debated funding priorities and passed the final version of the appropriations bill.

The problem States are having in adjusting to a constantly shifting mosaic of Federal budget and tax plans is made all the more difficult and frustrating by a basic difference in Federal and State fiscal years. Forty-eight of the 50 States operate on a different fiscal year than the Federal Government with most, like Georgia, using a fiscal year beginning July 1. This means that the dramatic changes in Federal grant funding and management, and the transfer of major program responsibilities to the States included in the Omnibus Reconciliation Act of 1981 have gone into effect 3 months into most States' fiscal year 1982 and many months more after the preparation of the State budgets for 1982.

In November of 1980, after many weeks of preparation with my Office of Planning and Budget, I had completed my budget recommendations to the legislature for the fiscal year 1982 that began July 1, 1981. In March of 1981, our legislature had completed the budgetary process and the budget was signed into law. With several months' lead time before the budget went into effect, agency heads were able to plan for implementation of the act beginning July 1, 1981.

Now look what happened in Washington.

In March, we looked at and analyzed the President's original budget proposals. In April, we poured over the House and Senate alternatives and looked up the definition of reconciliation. In May, we had the budget resolution and reconciliation instructions adopted by Congress. In June, our photocopying expenses soared as we passed out to our budget analysts the Senate and House reconciliation bills, each running well over a thousand pages and affecting the entire landscape of Federal-State relations. At about the same time, the administration proposed a series of rescissions and deferrals for fiscal year 1981, again changing every underlying assumption of a State budget already adopted almost a year previously. Then in July came the President's thousand-page-plus reconciliation floor substitute coupled with a plan to "cap" Federal medicaid contributions, soon followed by the supposedly final congressional conference report.

In July and August we went through the same process of adjustment and sheer guessing with the Federal tax cut bill, portions of which would be automatically incorporated into our State tax code.

Just as we began our budget hearings for fiscal year 1983, we learned that the President was proposing additional cuts in largely unspecified areas for Federal fiscal year 1982 and deferrals of previously appropriated funds. In addition, I understand the Senate is considering its own package of additional budget adjustments for fiscal year 1982. Finally, all of this current effort may prove to be moot when the administration adjusts its forecasts and economic assumptions in December.

As I have just stated, most States are now working on budgets for fiscal year 1983, with, as yet, no real certainty as to what funds will be available for the

remainder of fiscal year 1982 and only the vaguest notion about new cuts in grants-in-aid, new block grants, new tax cuts or increases, or entire new areas of government to be shifted to the States.

I would like to comment briefly on the havoc that Federal budget cuts within existing State budgets cause to existing and operating programs. These cuts made at the Federal level on State budgets don't automatically take effect. If the cuts are made in the middle of the State fiscal year, the magnitude of the cut on services is doubled because only a half year remains to make up the cut for the entire fiscal year.

If, in the last quarter of the fiscal year, we are told to cut $50 million from a program, we thus have to reduce our level of services by $200 million for the remainder of the fiscal year in order to pick up the $50 million. This means we have to displace employees and disrupt the program for the remaining three months. Then, in the next fiscal year, we have to crank up the program to a level of $150 million in order to maintain the $50 million cut. It simply makes no sense to yo-yo State budgets and the recipients of services with this type of manipulation of programs.

This problem is compounded by the fact that we have Federal restraints prohibiting us from immediately making these cuts.

For instance, take medicaid. It was necessary for me to cut $67 million out of medicaid after this fiscal year had commenced. Federal regulations required us to give a 60-day notice of any program changes that effectuate these cuts. With the other bureaucratic requirements, it takes a total of 90 days after the proposed cuts are made before they can go into effect. This is not the only type of delay we face. Five States, after proposing cuts, were enjoined by the courts.

Much has been said about the block grants and the latitude given to the States for making cuts. But during the entire debate in the Congress, all of us sat back knowing how much the cuts would total but we could only speculate on what latitude we would have after some of the categorical programs were combined into block grants. We could not react with our State budgets in making the proposed cuts until after final action. With each day of deliberation and debate in the Congress we were given less latitude.

The States have long maintained that with increased flexibility we could manage Federal programs more efficiently and responsively. Initially, block grants appeared to hold considerable promise as a method to provide Governors with this flexibility. The reality of block grants, however, has not lived up to that promise.

First, the timing of the block grants had made implementation extremely difficult. The Omnibus Budget Reconciliation Act of 1981 was signed into law on August 13, 1981. State administrative staff were first briefed by the Federal agencies on August 31, and we were expected to submit plans by October 1. In addition, funds were reduced substantially after one-fourth of our State fiscal years had already passed.

Of the more than 500 categorical Federal grant programs, only 57 programs have been consolidated into nine block grants. Thirty-three programs were collapsed into the elementary and secondary education grant and nine programs were collapsed into the preventive health block grant. If you eliminate these two block grants, you can see that the remaining seven block grants only represent a consolidation of 15 categorical programs.

Even with these few new flexible grants a great many restrictions remain. For example, we can transfer seven percent from the health prevention block grant but only to the alcohol grant, the primary care grant or the maternal and child health grant.

However, we can only transfer three percent in the first nine months and the remaining four percent in the last three months. This means that in this State fiscal year, I have the flexibility to redirect $91,530 out of an available $3,051,000.

In the alcohol, drug abuse and mental health block grant, States must allocate funds between mental health and substance abuse services in the same proportion as Federal funds were used previously. In the next year we get five percent discretion and the next year 15 percent flexibility. In addition, we have to use 35 percent of the alcohol and drug funds for alcohol and at least 35 percent for drug abuse services. Moreover, 20 percent of the alcohol and drug money must be used for prevention and early intervention.

I've tried to outline some of the problems we are experiencing at the State level and our difficulty in balancing a State budget.

I want to make it infinitely clear that we are aware of the enormous task which this Congress and this administration are facing. We are aware of the fact that the necessary action cannot be taken to address our national economic ills according to some previously prearranged time-table. Some uncertainty is inevitable. We are going to do the best we can at the State level under the circumstances we find ourselves in today. However, I come before you today and I plead with you to consider the proposal I am about to make.

I suggest to you, Mr. Chairman, that these problems that are being passed down to the States are unavoidably your problems, the President's problems, and the country's problems.

In the next few years, if the Federal budget is ever to be balanced, Congress and the administration will have to take on the major attempt to control the burgeoning cost of entitlement programs, several of which, particularly medicaid and welfare, the States share responsibility for financing and managing. This effort will require very close consultation and coordination between the States and the Federal Government or it will fail because, unfortunately, controlling the actual costs of a program out in the field is not simply a matter of drafting and fine-tuning budget numbers in Washington.

I strongly believe the States can and will serve a vital role in helping to balance the Federal budget and in assuming a variety of responsibilities previously performed at the Federal level. But we can do nothing but react on a piecemeal basis if no long-term plan is adopted with full consultation of everyone involved and then kept in place long enough to give it a chance to work.

To date, there has been no true prior consultation on New Federalism and other budget cuts with the Governors by the administration though I do credit Rich Williamson and his staff at the White House for making a yeoman's effort in our behalf. Unfortunately, too many in the administration view consultation as an after-the-fact briefing on what is to be submitted to Congress often only hours before the submission.

Many Members of Congress have listened to our concerns and recommendations, like Bob Dole on medicaid and the members of this subcommittee on block grants, and especially Sam Nunn and Mack Mattingly on important issues like waste-water treatment.

I think you must have noted the bipartisan nature of the Governors' concerns and suggestions throughout the past years and even today. We are not here to whine. We are not here to beg. We are here to say that we understand the complexity of your task and that we can and do understand what our respective and collective constituents want.

We share with you the desire to balance the Federal budget, the long overdue need to eliminate waste at every level, the absolute necessity to eradicate duplication of effort and unnecessary paperwork.

But, Mr. Chairman and members of this subcommittee, this cannot be accomplished in a vacuum.

I think it's time that we had a domestic economic summit involving the President, the bipartisan leadership of the Congress and our leadership so that we might gain general agreement on ultimate prime responsibilities for Government programs, the budget targets we should all plan for, and the time frame in which we are going to reach these goals.

The mood of this Congress and the mood of the people is to balance the Federal budget and curtail Federal programs. But the members of this subcommittee, Congress as a whole, and this administration know that we are talking about $80 to $100 billion in unidentified cuts that will have to be made if the Federal budget is to be balanced in 1984 and 1985.

This is an enormous responsibility. But, I stand here on behalf of the Governors and I pledge to this subcommittee and to the Congress and to this administration that we will do our part if we are given the opportunity to participate.

PREPARED STATEMENT OF GOVERNOR MATHESON

Mr. Chairman, in my testimony today I will draw heavily upon my experience as Chairman of the Subcommittee on Water Management of the National Governors' Association. The scope of these remarks, however, will be considerably broader than the issues discussed by the Water Management Subcommittee. My comments rely upon the work of other governors in areas such as transportation, community development, energy and natural resources. They also draw upon important information developed by the Council of State Planning Agencies. I

would like to address, in some detail, the impacts of the Administration's Economic Recovery Plan upon the nation's public capital stock—its infrastructure—a series of impacts which I believe will seriously worsen an already critical situation.

The nation's governors agree that appropriate steps must be taken to spur the economy and to provide the means by which the private sector can enhance investment, productivity and employment levels to boost profitability. Although considerable attention in the recovery plan has been focused on the decline of the nation's private capital stock, such as aging plants and equipment in the automobile and steel industries, the deterioration and wear of the nation's public capital stock have been virtually ignored. Failure to pay appropriate attention to our public facilities now threatens to seriously undermine the initiatives being taken to revitalize the economy.

A recent special report in Business Week entitled "State and Local Governments in Trouble" stated the following: "So serious is the decay of the nation's infrastructure and so poor the prospects for its refurbishment that many sophisticated businessmen and economists believe the U.S. is entering a period of severe crisis for state and local governments. . . . It is perfectly true that the private sector has carried the responsibility for economic growth throughout the history of the nation. But at virtually every stage of the nation's history, growth was dependent on a balance between private and public investment."

During the past decade, the nation's public facilities have been wearing out faster than they have been replaced. This translates directly into serious impediments for economic recovery. Let me give you some specific examples:

The Interstate highway system, the keynote of our national transportation network and only now approaching completion, has deteriorated to the point where almost one of every four miles of the system and 13 percent of its bridges are now beyond their service life and must be rebuilt.

Conservative estimates of the cost to rehabilitate and reconstruct our non-urban highways to maintain existing levels of service will exceed $700 billion during the 1980s. Even excluding the estimated $75 billion required to complete the remainder of the Interstate system, the balance required is still greater than all the public works investments made by all units of government during the 70s. Continuation of present investment levels will permit less than one-third of these needs to be met in this decade.

The funds required to meet the water quality needs mandated by the Clean Water Act presently exceed $120 billion for a program which the Administration proposes to limit to only $23 billion. Inadequate sewer lines and treatment plants are already stalling economic activity both in stagnating cities and in growing areas. Waste water treatment plants in 47 percent of America's communities surveyed in 1978 were operating at 80 percent or more of capacity. This means that new business plants as well as new homes cannot be hooked up to these systems.

Water resource development will require major investment in all regions of the nation in the 80s. Agriculture in the old "Dust Bowl" region will be in jeopardy toward the end of the decade unless new water sources can be developed to replace sources now being depleted. Reversion of this region to low yield dry land farming would devastate the economics of six states. In the arid West and Southwest, much of the nation's future energy must be developed in the form of coal, oil shale and petroleum. Energy development consumes vast amounts of water for both production and for the populations of impacted towns. In the water surplus areas of New England, New Jersey and New York, serious water crises are caused, in part, because of major inadequacies of water supply, storage, treatment and distribution systems.

One quarter of the nation's 1500 prisons are so antiquated, crowded and inadequate that riots are a constant threat. Crowded conditions are causing judges to require the early release of criminals to make room for new inmates.

One of every five bridges in the U.S. requires either major rehabilitation or reconstruction. The U.S. Department of Transportation has estimated that this could cost as much as $41 billion.

Municipal water supply requirements total between $75 billion and $110 billion to maintain present systems in the nation's 756 urban areas.

Reliable estimates of the investments required to rebuild the deteriorating roadbeds and rolling stock of the nation's railroads are not available. Similarly, we lack useful estimates of the cost of modernizing the nation's port and harbor facilities. But these key facilities are crucial to the national effort to export energy, food and other goods.

These are neither isolated nor extreme examples. I could cite many others. America's public works are wearing out in every part of the country in both suburban and urban areas, in areas of population decline and of rapid growth.

Unless these trends are reversed, the nation will end the decade with substantially fewer public facilities in usable condition—parks, libraries, bridges, reservoirs, highways, courthouses, fire stations—than exist today.

Of greater import to the discussion today, the condition of our public facilities seriously threatens the Administration's program for economic renewal. Over half of the nation's communities cannot permit expansion of firms or construction of new plants because community water and waste water treatment facilities are at or near capacity. Another quarter of the nation's communities are unable to improve their economies because other public facilities such as roads, bridges, industrial waste disposal sites, etc. are either worn out, obsolete or operating at full capacity.

The principal cause of the current decline in our public works has been long term under-investment. Because of tight budgets at all levels of government and high rates of inflation, maintenance of vital public facilities has been deferred. Replacement and rehabilitation have been postponed. New construction has been cancelled or stretched out.

No matter how the problem is measured, the evidence is clear: Total public works investment in non-inflated dollars fell from $33.7 billion in 1965 to less than $25 billion in 1979, a real decline of 28 percent. On a per capita basis, public works investment in constant dollars dropped from $174 per person in 1965 to $111 in 1979, a 36 percent decline. Measured against the value of the nation's gross national product (GNP), public works investment declined from 3.6 percent of GNP in 1965 to 1.7 percent in 1979, a 53 percent decline.

This condition is alarming. It is clear that public facilities are essential to our economic well being. The administrator of the former Bureau of Public Roads during the 1920s perhaps said it best: "We were not a wealthy nation when we began improving our highways, but the roads themselves helped us create a new wealth, in business, industry and land values. So it was not our wealth that made our highways possible. Rather, it was our highways that made our wealth possible."

To this rather depressing picture, we must now add the effects of the current economic package. In what I am sure is a largely unintended fashion, the Administration's economic program will further exacerbate the crisis in public facilities.

1. Specific budget cuts proposed by the Administration and generally being adopted by Congress will result in a substantial reduction in direct federal investment in public infrastructure. The Omnibus Budget Reconciliation Act will cut programs in transportation, sewer grants and community development by $4.8 billion in FY 82 alone, or 22 percent of current expenditure levels. This figure may be low depending upon the final outcome of the battle for a $2.4 billion appropriation for sewer grants this year. This underscores an absolutely critical issue. It is impossible for states and local governments to rationally plan public works investment given the extraordinary levels of uncertainty induced by the present budget cutting process.

2. The federal tax cut aimed at spurring incentives to the private sector to invest in their own plant and facilities also results in reducing revenues available to state governments which themselves provide another major source of public facilities investment. An analysis of the impact of the federal tax cuts on the states indicates that the cuts in personal and corporate income taxes coupled with new depreciation rules and the "'All Savers" interest exemption will result in net state revenue losses and additional borrowing costs to $2.3 billion in FY 82. Once again, the intergovernmental consequences of federal action appear to have been ignored or inadequately considered.

3. High interest rates triggered by federal budget deficits and tight money policies have forced many states and local governments out of the credit markets. This year the total amount of tax exempt municipal bonds issued is expected to register the largest drop in a decade from $48.3 billion to about $41 billion. Of this total amount, about $10 billion a year has been used for infrastructure investment and it has been slowly declining in real terms during the decade. National policy now pits state and local governments desiring to invest in infrastructure squarely against the economy's most powerful borrowers—the federal government and large business corporations.

4. Other cuts in the federal grants-in-aid system, in programs ranging from health care to job training, will also have a devastating effect on infrastructure investment. The reason is that states and communities will inevitably use their own diminished revenues to replace cuts in high priority services—police and fire departments, education, public transportation, and health care. Thus, the present and proposed budget cuts in other areas are likely to further accelerate

the long-term decline in infrastructure as public works are either deferred or postponed.

It is important to note that many of the budget cutbacks proposed and now being enacted have been offered in the name of "New Federalism," a term which we have presumed would mean some intergovernmental sorting out of the responsibilities and authorities of the national, state and local governments. The nation's governors clearly support the concept of transferring many present national programs to the states. For example, the Subcommittee on Water Management has developed, and the governors have adopted, a specific policy on sewer grants. In that policy, we have taken the position that the federal government does not have a responsibility to fund construction of waste water treatment plants in perpetuity. However, we believe that the mandate must be reasonably relaxed or terminated, that significant program reforms are necessary to reduce administrative burdens and to cut construction delays and that the program must be phased down with a stable level of funding over a determinate period of time to provide the certainty necessary to handle the transfer. The same approach could be used in other programs dealing with capital facilities.

As another example, discussions are now taking place regarding a possible turnback of a portion of an increased federal gasoline tax to the states in exchange for them assuming most transportation programs other than the Interstate System. Such a turnback program could provide immediate increases in investment levels by both the states and the federal government as well as improve the overall fiscal condition at both levels of government.

Unfortunately, most of what has been transferred to the states to this point has been responsibility for presiding over major cutbacks in key program areas without a parallel federal assumption of programs primarily national in character. What is urgently needed, in my judgment, is a recognition that economic revitalization is a cloth made of interwoven threads. An important set of those threads are the intergovernmental investments in public facilities which support expansion and revitalization of the private sector. The Administration and Congress, as well as the state and local governments, must recognize the serious condition of our nation's infrastructure and its importance in supporting economic growth. We must jointly develop an intergovernmental approach to address the need to repair, replace and rebuild these important facilities. Some suggestions in these areas follow:

We must develop a strategy which substantially cuts delays, mismanagement and fraud in public works.

We must craft an intergovernmental approach to provide funding certainty and additional flexibility in each of the federally assisted capital facilities programs to meet the highest priority infrastructure problems within each program and each state.

Serious consideration should be given to developing a series of functional block grant programs for capital facilities investment.

Hearings and discussions should begin on ways in which transfer of responsibility for these programs can be accompanied by federal assumption of other responsibilities, revenue turnbacks or both. I should note that it is not sufficient for the Administration to reduce levels of taxation and then suggest it has done its part in providing for revenue turnbacks. This encourages officials in the executive and legislative branches of state and local government to attempt to outdo the Administration and the Congress in cutting programs and limiting taxes and expenditures. The net result is a diminished fiscal capacity on the part of state and local government to adequately carry out the transfer of authority which is a centerpiece of the Administration's political and economic philosophy.

One thing is clear, a nation which neglects to maintain and revitalize its public facilities cannot hope to remain a dominant economic force in a mixed economy where success in the market place is so closely tied to the public setting within which the economy operates. The issues are clearly joined.

Leadership is badly needed at the federal level to:

(1) Develop estimates of present and future costs of addressing the most critical public facilities problems facing the country;

(2) Determine which level of government is best suited to take responsibility for each problem area; and

(3) Establish financing authority and program responsibility to reflect and implement these decisions.

Senator DURENBERGER. The hearing will now be adjourned.

[Whereupon, at 12:05 p.m., the subcommittee recessed, to reconvene subject to the call of the Chair.]

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